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NOMINATIONS OF DAVID C. MULFORD AND ROBERT R. GLAUBER

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

THE NOMINATIONS OF

DAVID C. MULFORD, OF ILLINOIS, TO BE UNDER SECRETARY FOR INTERNATIONAL AFFAIRS OF THE DEPARTMENT OF THE TREASURY

AND

ROBERT R. GLAUBER, OF MASSACHUSETTS, TO BE UNDER SECRETARY FOR FINANCE OF THE DEPARTMENT OF THE TREASURY

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NOMINATION OF DAVID C. MULFORD, OF ILLINOIS, TO BE UNDER SECRETARY FOR INTERNATIONAL AFFAIRS OF THE DEPARTMENT OF THE TREASURY

FRIDAY, MAY 12, 1989

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The committee met at 9:05 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Donald W. Riegle (chairman of the committee) presiding.

Present: Senators Riegle, Sarbanes, Wirth, D'Amato, and Pressler.

OPENING REMARKS OF CHAIRMAN RIEGLE

The CHAIRMAN. The committee will come to order. We are starting at an earlier hour this morning to accommodate several scheduling requirements. We are pleased to have Mr. Mulford with us at this time. He has a hearing later in the morning before the Finance Committee which we are mindful of, and so we will proceed apace here.

Senator D'Amato is with us and we will have other members coming in the course of the morning. We have other items, including the FSX, which of course is a major interest of Senator D'Amato's as well, which may take him away here at some point.

I have an opening statement that I want to make here in a minute before we go to our witness, but Senator D'Amato, did you have a comment that you wanted to make at the outset?

Senator D'AMATO. Yes, Mr. Chairman.

I am delighted to welcome our nominee before the committee. He seems to have a distinguished record. I would hope that we would approve his nomination speedily. Having said that, I would ask that my full statement be included in the record as if read in its entirety.

The CHAIRMAN. Without objection, so ordered.

OPENING STATEMENT OF SENATOR D'AMATO

Senator D'AMATO. Mr. Chairman, I welcome Mr. Mulford and Mr. Glauber to the Banking Committee. Neither of these gentlemen's names are strange to this committee. Indeed both of their names are associated with major initiatives which have come out of the Brady treasury.

While we are aware almost to saturation with Mr. Glauber's principal product, the Bush Thrift Plan, we have yet to fully understand the new Secretary's, and Mr. Mulford's, ideas on Third World Debt.

As you know, Mr. Chairman, debts owed to this country's commercial banks by lesser developed countries are problems of enormous complexity. This situation is the focus of a great deal of study and many proposals for dealing with "the Third World Debt problem." But we must remember that "Third World Debt" is not a single problem, subject to a single sweeping solution any more than any other complex problem is susceptible of a simple solution. The various developing countries which are carrying large levels of debt to commercial banks have complex economies and all the problems of regulating those economies and promoting growth. For each country that has more debt than it believes it can service there is a separate and multifaceted problem.

The Third World Debt plan of Mr. Brady's predecessor, James Baker, emphasized the case-by-case approach necessary to deal effectively with LDC debt. I have seen nothing in the past few years to change my belief that each country is its own case.

I am particularly concerned at the talk of dealing with LDC debt burden as a separate problem. This country's goal should be to promote democratic government, free market economics and sound management of each LDC country. Debt burden is only a symptom in many cases. Elimination of all foreign debt will accomplish nothing absent sound political and economic structures in these countries. We need to appreciate the broader problems as well as the complaints of the debtor countries.

I am certain that Mr. Mulford appreciates these complexities. Therefore, I look forward to better understanding the Brady Plan as it takes shape.

Thank you, Mr. Chairman.

OPENING STATEMENT OF CHAIRMAN RIEGLE

The CHAIRMAN. I have called today's hearing on the nominations of David Mulford and Robert Glauber to be the Treasury Department's only two Under Secretaries because both nominees will, in their new positions, exercise important responsibilities on matters that are clearly within the Banking Committee's jurisdiction.

When these nominations were submitted by the White House to the Executive Clerk of the Senate, they were routinely referred to the Finance Committee, a committee of which I myself am a member, because as a general rule all Treasury nominees, with certain limited exceptions, are sent to that committee for confirmation.

After these initial referrals, however, our staff examined the principal duties of each of these nominees and it became clear that many of them concern matters that are of great and direct importance to this committee.

Rule 25 of the Standing Rules of the Senate states that the Banking Committee has jurisdiction over matters dealing, among others, with "banks, banking and financial institutions, deposit insurance, economic stabilization and defense production, export and foreign

trade promotion, export controls, Federal monetary policy, and money and credit." The Rules also give the committee responsibility for "international economic policy as it affects U.S. monetary affairs, credit and financial institutions."

Mr. Mulford has major responsibilties for international economic policy coordination, including exchange rate movements for international debt policy, for international trade in financial services, and for review of investment flows to our country. These are all matters within the jurisdiction of the Banking Committee and upon which we in fact legislated in the Omnibus Trade Bill of 1988.

Obviously, each of these matters is of very significant importance to our country. Mr. Mulford is the Treasury Department's first Under Secretary for International Affairs, which demonstrates Treasury's recognition of the importance of these issues. Our committee is already very familiar with Mr. Glauber and I will make other comments about his situation when we take him up, following our discussion with Mr. Mulford.

In recognition of our committee's very direct interest in the assigned work of these nominees, Senator Bentsen, Chairman of the Finance Committee, which has already acted favorably upon these nominees, agreed to not have the Senate as a whole pass on these nominations until our committee had had the chance for today's hearing. And I want to publicly thank Senator Bentsen for his courtesy and his comity in this situation.

Before we go on, I have statements from Senators Dixon and Garn to be inserted in the record.

STATEMENT OF SENATOR ALAN DIXON

Senator DIXON. Mr. Chairman, I am pleased to be here this morning as the Senate Banking Committee conducts hearings on the nominations of David C. Mulford, to be Treasury Under Secretary for International Affairs, and of Robert R. Glauber, to be Treasury Under Secretary for Finance. I note that Mr. Mulford is a son of the great State of Illinois, and welcome both gentlemen before the committee.

I have served on the Banking Committee for the almost 8½ years that I have served in the Senate. I do not recall a year when the committee had more major legislative issues before it. From the FSLIC bill which the Senate just passed, the international debt policy changes which are in process, the Glass-Steagall reform/financial modernization bill which I introduced in January, to competitiveness, market reform and consumer issues, I believe we all have our work cut out for us this session.

I hope that the witnesses today will outline, in necessarily broad terms, the administration's goals with respect to these important issues. In particular, I would like to know whether the administration is committed to expeditious consideration of the financial modernization bill.

I look forward to working with Under Secretary Designees Mulford and Glauber on all of these issues. I hope that the Treasury Department will remain committed to the bipartisan spirit in which the Banking Committee has been able to operate thus far this year.

Thank you, Mr. Chairman.

OPENING STATEMENT OF SENATOR GARN

Senator GARN. Today the committee will consider the nomination of David C. Mulford, to be Under Secretary of the Treasury for International Affairs, and Robert R. Glauber, to be Under Secretary of the Treasury for Finance.

It is important to note that, while these nominations have not been formally referred to the Banking Committee at this time, the positions to which these gentlemen have been appointed are squarely within the jurisdiction of the Banking Committee. Under normal circumstances there would have been a joint referral of these nominations to this committee and to the Finance Committee. But it is necessary to move these nominations along. These two positions have been vacant for too long. Fortunately, Mr. Mulford and Mr. Glauber have already been serving, but it is time that we give them the full benefit of confirming them in their jobs. I note that the Finance Committee earlier this week reported these nominations to the Senate, favorably I might add, and I hope for and expect speedy action by the Senate on these nominations.

David Mulford is no stranger to this committee or to his job. He is now perhaps the most senior member of this administration, at least from the point of view of experience, in dealing with the important international financial issues facing our country. He is well respected around the world as well as here in the United States. We are fortunate that we can still have his services. Advancing Mr. Mulford to the rank of Under Secretary only recognizes the role that he has in effect played for many years.

Robert Glauber is becoming less and less of a stranger to this committee. He has already had his sleeves rolled up and been involved in formulating administration policy on financial institutions issues for several months, not the least of which has been his involvement in the Savings and Loan legislation. It is a tribute to this administration and Mr. Glauber's work that the administration's savings and loan legislative package has, in nearly all of its essentials, remained unchanged by either the House or the Senate as it has been considered so far. I look forward to working with Mr. Glauber in the weeks and months to come. If anything is clear, it is that it takes many people working together to deal successfully with the issues facing our nation's financial institutions.

Thank you, Mr. Chairman.

The CHAIRMAN. Increasingly, it seems to me, that as we globalize the economy, as the United States is integrated more and more into the global economy, the divisions of responsibility between committees are no longer nice, neat, orderly lines of separation. Work areas and Cabinet offices now cut across a number of functional areas of jurisdiction within the Senate. We certainly find that true between our committee and the Senate Finance Committee.

Senators Heinz and Roth, who also serve here and on the Finance Committee, have a chance to see that directly, as do I as member of both those committees. And so it is in this fashion that

we hope to be able to handle, at least for now, this question of jurisdiction, of work that falls in more places than one.

So we are pleased to have with us Mr. Mulford today. And I would like initially, Mr. Mulford, to ask you to make any comment that you might wish to make, and I would also ask you, if you don't otherwise plan to, to give us a sketch of your own professional background that leads up to your very important appointment to this position.

STATEMENT OF DAVID C. MULFORD, NOMINEE TO BE UNDER SECRETARY FOR INTERNATIONAL AFFAIRS OF THE DEPARTMENT OF THE TREASURY

Mr. MULFORD. Thank you. Mr. Chairman.

I appreciate the opportunity to be here today before this committee to answer any questions you may have with regard to my role as Under Secretary of the Treasury for International Affairs in international economic policy formulation in the Bush Administration.

I have submitted in advance a brief statement of my views on several major areas of international economic policy and would be happy to respond to questions you may have on these issues. I would also be grateful if a copy of that submission could be put into the record.

The CHAIRMAN. It will be.

Mr. MULFORD. In my brief oral remarks this morning, I would like to express my gratitude to three people for their confidence and support.

First, I am deeply honored to have been nominated by President George Bush for the position of Under Secretary of the Treasury for International Affairs, and will seek with all my energy to fulfill his expectations.

Second, I want to say how much I have enjoyed working with Secretary of the Treasury, Nicholas Brady, since his arrival at Treasury in September last year. I admire the important job Secretary Brady has done in the early months of the administration, and wish here to express my thanks to him and my full support for his efforts.

Finally, I would also like to mention my wife, Jeannie Simmons Mulford, who, in addition to the outstanding job she has done for the past 17 years as a flight attendant for United Airlines, gives me the support and affection essential in public life. Unfortunately, she can't be here today with the short notice—she hardly ever misses a hearing—because in fact she's flying.

As you know, I have served as Assistant Secretary of the Treasury for International Affairs for the past 5 years, working closely with three Secretaries of the Treasury. During that time, I have concentrated my energy on developing strategies for several specific areas of international economic policy.

My experience in general has confirmed one very important principle: The United States cannot solve international economic problems alone, in the complex and interdependent world that we are faced with today. We must first determine our primary interests, know our objectives, and develop our particular strategies—

and consultations with Congress are of course essential to this task—but it is only through close cooperation with other nations that we can hope to generate an international economic environment conducive to our success.

In the coming months, I will concentrate my attention on three main areas of international economic policy; namely, economic policy coordination between the major industrial nations; the international debt strategy; and issues concerning international trade and investment.

I believe we have seen significant accomplishments in these areas in recent years, more reflective perhaps of congressional concerns than when I first arrived in Washington. I have found it deeply satisfying to have played a part in these past few years in our country's international economic policies and look forward to making a further contribution as Under Secretary in the Treasury.

Mr. Chairman, you asked me to make a brief summary of my experience prior to this time, and let me do that in just a few brief sentences. I was born and raised in Rockford, Illinois, went to public high school there; was a serious athlete throughout my high school and college days. I went to college at Lawrence University in Appleton, Wisconsin. I followed that with a scholarship to the University of Cape Town in South Africa, a Rotary International Fellowship. I spent 1 year in South Africa.

I then returned to the United States and completed an M.A. degree at the African Studies Program at Boston University, and I followed that with a Ph.D. at Oxford University in England at St. Anthony's College, where I concentrated my efforts on African economic and political developments in East, Central and Southern Africa.

When I finished at Oxford, I was nominated and won a White House Fellowship in the first year of the White House Fellowship Program, 1965–66, and I served that year as Special Assistant to the Secretary and the Under Secretary of the Treasury, then Joe Fowler and Joe Barr, who was Under Secretary at that time. That is where I began to establish my first interest in international economic matters.

I then went to Wall Street and joined White Weld and Company, investment bankers, which was the most international firm among the American investment banks at the time in the early days of Euro-markets. I worked with that firm until, in 1978, it was acquired by Merrill Lynch, and I stayed with Merrill Lynch until I came to the Treasury in 1984.

However, in 1974, as a member of White Weld, I went out to Saudi Arabia to head up a team of people from White Weld and Company and Bearing Brothers in London and the Merchant Bajk in London, tk provide investment advice and to create an investment program for the Saudi Arabian Government for the investment of their excess oil revenues. I went there in 1974 when those large revenues were just accumulating and I stayed for 10 years managing a portfolio which ultimatehy rose to $130 billion and was invested worldwide in many markets around the world.

I stayed there until early 1984 when I came back here to become Assistant Secretary of Treasury for International Affairs.

[The complete statement of David C. Mulford follows:]

EMBARGOED UNTIL DELIVERY
EXPECTED AT 9:00 A.M.
FRIDAY, MAY 12, 1989

STATEMENT OF
DAVID C. MULFORD
NOMINEE FOR
UNDER SECRETARY FOR INTERNATIONAL AFFAIRS
UNITED STATES DEPARTMENT OF THE TREASURY
BEFORE THE COMMITTEE ON BANKING,
HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

I appreciate having this opportunity to appear before this Committee and respond to questions you may have with regard to my role in international economic policy in the Bush Administration. I am also honored to have been nominated by President George Bush for the position of Under Secretary of the Treasury for International Affairs. I would like to say at the outset that I intend to continue working closely with Members of Congress in general and with this and other Committees in the Senate and House with jurisdiction over international economic policy. Many important international economic issues face the United States at this time. They will require close consultation between the Administration, in particular the Treasury Department, and key Congressional Committees. I am committed to this cooperative process and look forward to the progress I feel sure we can make on these issues.

I have served as Assistant Secretary of the Treasury Department for International Affairs for the past five years, working closely with three Secretaries of the Treasury. During that time I have concentrated my energy on developing strategies for several specific areas of international economic policy. My experience has taught me one overriding lesson: the United States cannot solve international economic problems alone in the complex and interdependent world that we are faced with today. We must determine our primary interests, know our objectives, and develop our particular strategies; but, it is only through close cooperation with other nations that we can hope to generate an international economic environment conducive to our success.

This has been a guiding principle for me in the main areas of international economic policy: namely, economic policy coordination between the major industrial nations, the international debt strategy, and international trade. I believe we have seen significant accomplishments in these areas in recent years that will influence positively our work in the period ahead.

International Economic Policy Coordination

Economic policy coordination, as practiced today, began with the Plaza Accord in September of 1985. By revitalizing the G-5 consultation process and conferring closely on both economic policies and the methods of more effective coordination, we were able to develop a unified view on the general policies required for adjustment. This included the need to realign the major currencies and to institute policies to reverse the rapid growth in our trade and current account deficits. In short, it was necessary to alter the fundamental economic conditions between surplus and deficit countries to promote global adjustment without undermining world growth and damaging world trade. The necessary currency adjustment was accomplished through several years of cooperative effort among the G-7 nations, without adversely affecting world growth. At the same time, we have made solid progress in the adjustment process in the form of substantial improvement in our trade and current account positions in 1988.

In 1986 and 1987, we negotiated a more formalized economic policy coordination process which was reflected at the Tokyo and Venice Summits. We have made important strides in using economic indicators to help focus discussion in the G-7 on developing medium-term objectives for our economies and helping to assess our progress. Our success these past few years has resulted in closer working relationships and greater regularity of consultations.

Obviously, further progress in adjusting external imbalances is essential for the long-term political and economic interests of the United States. All the major trading nations need to strengthen domestic policies to promote more openness and adjustment. Here in the United States our primary policy objective must be further reduction of our fiscal deficit.

Newly Industrializing Economies

During the 1980s new industrial players emerged on the world economic stage. The so-called newly industrializing economies (NIEs) of Asia grew rapidly and, through the pursuit of export-oriented policies, increased tremendously their share of world trade. By mid-1986 -- some nine months after the Plaza Accord, it was clear that we would face a major problem with the NIEs. In 1987, our bilateral trade deficit with the four most prominent NIEs reached nearly a quarter of our total trade deficit.

While recently there has been some reduction in their surpluses, the pace is very slow. This is due in part to their exchange rate policies which, in the case of Korea and Taiwan, we

have sought through negotiations to change, so that their respective exchange rates reflect more accurately the underlying strength of their economies. Through frequent bilateral talks, speeches, and by focusing attention on these economies in two recent Treasury reports to Congress on international economic and exchange rate policy, I and my staff have worked to improve this situation. More intensive negotiations during the past six months have accomplished further movement. Nonetheless, additional efforts, I hope supported by this Committee, will be necessary to obtain greater cooperation and adjustment, in particular by Korea and Taiwan.

International Debt Strategy

Turning to the international debt strategy, you are all familiar with the proposals put forward by Secretary Brady on March 10 to the Bretton Woods Committee. These proposals address what is perhaps the most complex international economic and political problem facing the U.S. today. Throughout the period I have been at Treasury, the international debt problems of developing nations have been a primary policy concern. Our objectives have been to promote economic policy reforms in debtor nations, to work with the IMF and World Bank in providing resources to support those reforms, and to stress the need for continued external financial support from all sources, including the commercial banks. We have approached debtors on a case by case basis, reflecting their great differences and seeking to fashion solutions tailored to each country's unique situation.

Although the principles cited above have consistently guided our efforts, the strategy has evolved significantly over the past five years. In early 1987, for example, Secretary Baker introduced the important concept for commercial banks of a "menu" of options for bank financing packages. This was designed to facilitate broader participation by banks in financing packages that recognized the banks' increasingly diverse interests and strategies. Commercial banks were encouraged to design more creative financial techniques which has helped to stimulate a range of instruments that can promote direct investment, restructure and reduce debt and debt service burdens. An important contribution to the development of debt reduction techniques was the Treasury's support of Mexico's 1987 debt swap transaction with commercial banks, collateralized by Treasury zero coupon bonds. I believe this transaction provided an important breakthrough in the debt reduction area which in various modified and improved forms will play a major role in future debt and debt service reduction developments. Several debtor nations have adopted debt/equity swap programs which we began advocating three years ago. This technique has also been further developed and supported in Treasury for debt-for-nature swaps to support environmental projects.

With the advent of a new Administration, it was necessary to conduct a thorough review of the debt strategy. Serious problems needed to be addressed. Reforms in the major debtor nations were not sufficient to provide sustained low inflation growth. Commercial banks were withdrawing, while being for the most part fully serviced as to interest, often with funds flowing from international institutions. The stock of debt and thus the debt servicing burden continued to grow. These and a variety of other long-term problems led Secretary Brady to develop proposals for strengthening the debt strategy. The proposals placed greater emphasis on growth-oriented reforms that expanded the role of market forces in the debtor nations' economies, as well as on creating incentives to encourage a stronger focus on voluntary, market-based transactions between debtors and banks that reduce debt and debt service. When implemented by the various participants, these proposals will produce more manageable new financing requirements, reduce the stock of debt and debt service, and help encourage additional economic policy reforms. Of course, credible economic policies and strong performance by the debtors themselves will continue to be the most essential element for long term success.

Finally, Mr. Chairman, I have had a continuing responsibility for trade and investment issues at Treasury these past few years. Although Treasury does not have the lead on trade issues, we make an important contribution and sometimes play a strong leadership role. It is occasionally forgotten that the world's trade problems are intimately related to international macroeconomic policy issues. If these can be addressed successfully by the major industrial nations, our chances of maintaining constructive and successful trade policies will be greatly improved. The technical side of trade and trade dispute issues are important, but they are not decisive for long-term success in preserving the world's free trade system. The macroeconomic policies of major trading nations in the end are decisive. Our strategy should be heavily weighted towards accomplishing these broader changes.

As an example, Mr. Chairman, I would cite the Yen/Dollar talks with Japan, which began in 1984. This dialogue serves as a model for successful negotiation of major structural changes in Japan, changes that have had a significant and I believe lasting impact on Japan's economy and its performance. Major progress was made in internationalizing the Yen, opening Japan's financial markets to U.S. financial organizations, and liberalizing Japan's internal capital markets. The changes were fundamental and are continuing to unfold. The Yen/Dollar approach was later used as a model for the so-called MOSS talks with Japan, which though not presently in use, is I believe an approach to trade problems that is essential for sustained success.

I look forward, Mr. Chairman, to working together with this Committee. Thank you.

The CHAIRMAN. Very good. That's a long record of very serious involvement in a variety of ways and a major economic foreign policy type activity.

I have a series of questions I want to go through. Senator D'Amato, I don't know what your time is this morning. Are there any items you'd like to raise at the outset here?

Senator D'AMATO. Mr. Chairman, as you pointed out earlier, there's a very interesting phenomenon that took place and I would like to just ask one question before I leave.

Mr. Mulford, the Washington Post report today that Citibank announced yesterday that it had applied about $80 million in deposits that it holds for Ecuador towards payment on a loan which was owed by that country. The Post further states that the Citibank action is tantamount to a seizure of assets and will intensify tensions between Third World countries and their bank creditors.

What do you think of the Citibank action and will it further complicate your efforts to make a go of the Brady Plan?

Mr. MULFORD. The Citibank action was taken with regard to Ecuador's failure over the past period of a year or more to service its debt; it Ecuador has large interest arrears which have built up to the banks. Citibank in this case took liquid deposits that it had from Ecuador in connection with a trade facility Citibank has with Ecuador, therefore outside the multibank medium-term credit agreement. So in doing that, Citibank was within its rights under its agreements to take that action.

On the other hand, my personal opinion is that the action was politically insensitive in many ways and has caused as major problem for the Ecuadorans. My hope is that the two parties can sit down and discuss the issue and see if they can work something out.

I don't think it is a serious problem for the Brady Plan per se. It does, of course, raise tensions on the one hand, but on the other hand it also illustrates how sensitive the issue of arrears are when countries allow these arrears to build up to the banks. The banks become very nervous about that and when they have an opportunity to take some action that is limited and rather surgical these things will happen.

So I hope we all learn a lesson from that, which would be that all parties work harder to move the debt proposals forward and get on with the job.

Senator D'AMATO. Mr. Chairman, I appreciate Mr. Mulford's candid appraisal. The fact that Citibank's action was probably at least politically insensitive.

I would like to at a later time, if we had more time, discuss in some detail how do we keep the flight of capital that goes from our banking system to Third World nations and right back out of those countries just as fast as it goes in. It seems to me an element of that which must be stressed, which I don't know what we are going to do to attempt to bring it about, is the kind of economic and social reform, economic reform within the countries who are going to be borrowing this money.

Lest there be meaningful economic reform—and I don't mean a curtailment of subsidies, et cetera—the kinds of things that are going to bring about revolutions, it seems to me that we are trying to micromanage in some of these areas—but, rather, much more

extensive and broad undertaking, encouraging capital and foreign investment in these countries, unless that is done we are going to continue to have flight of capital from these countries to the Swiss banks, et cetera, and the debt is going to go higher and higher.

I have not seen manifested, other than just some utterings from the Mexicans, that there is going to be this kind of realization and undertaking, of really trying to create the climate—political stability is one of them—but encouraging foreign investment that is going to bring about the essential change.

If you want to comment on that, fine.

Mr. MULFORD. Just briefly. I, in fact, agree with what you've said. The proposals that we have made for strengthening the debt strategy have as an important part of them a stronger recognition by the Fund and by the Bank and by the countries, of the necessity to deal with the flight capital problem and to undertake, through policy changes of the type you mentioned, more open investment policies but also a better range of macroeconomic policies as well, policies that will encourage the return of capital.

In the long run, capital flight will be reversed only if the countries undertake the kind of broad policies on a sustained basis that restore confidence among their own people to keep their money at home. In a way, that is a good judgment to whether or not the country is succeeding. We think countries need to be more sensitive to this issue and we've placed it as a very high priority.

If capital flight problems are not addressed because underlying policies are incorrect, then I think it's fair to say there are not enough resources around to solve their problems because, as you say, whatever arrives from outside will go out the back door. So it is a very, very important problem.

Senator D'AMATO. I thank you very much.

Mr. Chairman, thank you for your courtesy.

The CHAIRMAN. Thank you, Senator D'Amato.

Time permitting, we will pursue that a little bit later. I, too, appreciate the frankness of your answers.

Now, Mr. Mulford, from the testimony that you have submitted to the committee, I understand you have key responsibilities within the Treasury Department obviously for international economic policy; but, namely, economic policy coordination between the major industrial nations, including attention to exchange rate movements, international debt strategy, international trade in financial services, and a review of investment flows into our country.

Now, I want to be sure that I have a correct understanding of what are, in fact, to be your principal duties and if that's what you see them to be.

Mr. MULFORD. Yes, that is correct.

The CHAIRMAN. Are there any other major duties that will occupy a significant portion of your professional time that I have not mentioned there?

Mr. MULFORD. Well, there are a number of subcategories to the ones you've mentioned that are very important. For example, our ongoing discussions with the Government of Japan on liberalization of financial and capital markets in Japan; the discussions that we have on a continuing basis with Korea and Taiwan on their currencies and on their economic policies; the question of more open

investment policies around the world, both among debtor countries and among the industrial nations.

Under the economic policy coordination heading, there is the ongoing relationship with the G–7 countries, where I am the Deputy for the Secretary and meet with my counterparts regularly. But in addition to that, there are many other policy coordination fora where I do attend, such as Working Party Three of the OECD, the OECD Ministerial meeting, G–10 meetings, and so on. So it's a wide area of policy that is covered, and those headings you gave are fairly broad and include a lot of subcategories.

The CHAIRMAN. I have a purpose in wanting to go through some other clarifications of this kind, so bear with me here.

Mr. MULFORD. Sure.

The CHAIRMAN. With regard to your responsibilities for economic policy coordination among the major industrial nations and, specifically, exchange rate negotiations, I take it that that is a very important part of your duties, and of course you testified here with Secretary Brady, pursuant to section 3005 of the Omnibus Trade Bill of 1988, just last week.

But is it fair to say that that exchange rate responsibility is a major part of your work assignment, as you understand it?

Mr. MULFORD. Yes, it is.

The CHAIRMAN. Can you give me a sense as to what part of your normal work time would likely go to those issues? And let me list that under the heading of economic policy coordination among the major industrial nations and exchange rate negotiations. Can you give a rough estimate?

Mr. MULFORD. Oh, it varies, but I would put it at around 40 percent perhaps.

The CHAIRMAN. And do you see that continuing at about that level of effort going ahead in the future?

Mr. MULFORD. Yes, I think it will.

The CHAIRMAN. You state that you have significant duties with regard to international debt policy, including implementation of the Administration's new debt strategy, the so-called Brady Plan.

We obviously have a very keen interest in that subject in terms of how that will relate to our own economic future. But can you tell me what part of your professional time would you say is now going to the so-called Brady Plan or sort of the debt management problem here?

Mr. MULFORD. I would say in response to that question, the debt strategy is a time-consuming area of activity. But, like policy coordination, it tends to fluctuate a bit. I would say that over the years, the debt strategy has occupied about 40 percent of my time. At the moment, it is occupying a considerably higher proportion of my time during this phase of implementation, probably closer to 70 percent for the time being.

I hope at the end of the day I don't have to make all these numbers add up.

The CHAIRMAN. No, I understand. And I appreciate the directness of the answer. I know it's difficult. Part of what I'm trying to do here, things have changed so much, the world has changed so much, and obviously you're in a new assignment and that's a recognition of the fact that we're trying to adapt, in a sense, administra-

tive Federal Government strategy to changing circumstances, and so it's not surprising to me that you would find that the time allocations are moving around.

I take it, then, that the debt plan, as it relates to outstanding bank loans to Third World countries has become a major preoccupation at the present time, and presumably then considerably more than half of your work time at the present time is in the area.

Mr. MULFORD. Yes.

The CHAIRMAN. In terms of looking forward, there is no way of knowing when that problem will resolve itself. But wouldn't it be fair to say that that's a problem that in one form or another is likely to be with us for some considerable period of time here?

Mr. MULFORD. Yes, that's right; for some years.

The CHAIRMAN. Now, you state on page 4 of your testimony, that the Treasury Department does not have the lead on trade issues. Are there any exceptions to this general rule?

For example, am I correct in my belief that the Treasury Department took the lead in negotiating the provisions of the U.S.-Canada Free Trade Agreement dealing with financial services—which, of course, this committee had jurisdiction over—but would that be the case?

Mr. MULFORD. Yes, that's right. And there are a number of other trade issues where the Treasury has played a lead role, such as in the MOSS talks a few years ago, where I chaired the pharmaceutical group, for example.

But, in general within the administration, the Treasury is not regarded as having the lead in trade. That is, as you know, USTR and Commerce.

The CHAIRMAN. Let me just touch on two more, and then I want to yield to my two colleagues who have come in here, very particularly the Chairman of the International Finance Subcommittee.

Am I correct also in understanding that the Treasury has the lead responsibility for the negotiations in the Uruguay GATT round, dealing with trade and financial services?

Mr. MULFORD. Yes, that's right.

The CHAIRMAN. Are the two Deputy Assistant Secretaries who take the lead on bilateral and multilateral trade and financial services under your supervision?

Mr. MULFORD. Yes.

The CHAIRMAN. Can you give us any sense as to what part of your time, at a minimum, would go to these matters?

Mr. MULFORD. Let me answer that with just a little bit of an explanation. The way in which trade issues seem to work is that the flow of individual product issues or negotiations is handled by members of my staff, working with other agencies that have the lead. The amount of time, therefore, that I actually put in on individual items is relatively modest because the work is done in committees elsewhere and the issues come up for decision on policy questions. So the time element is not so large there.

However, there is a larger expenditure of time on what I would call trade strategy, the general issues of trade strategy. That comes and goes, but I would put that, therefore with that sort of weighting, I would put 10 to 12 percent on trade and investment matters.

The CHAIRMAN. I have a few other questions along these lines that I want to pursue, but let me now yield to Senator Sarbanes, chairman of the Subcommittee on International Finance and Monetary Policy.

Senator SARBANES. Mr. Chairman, I appreciate that. I will be very brief. I have another hearing that I have to be at, unfortunately. But I wanted to be here for a couple of reasons.

First of all, I am very pleased to welcome Under Secretary Designate Mulford here this morning before the committee. We have worked closely with him over the past 5 years in his role as Assistant Secretary of the Treasury for International Affairs, and I must say I am supportive of the—in a sense—upgrading of this office to an Under Secretaryship. I think, obviously, the matters under his jurisdiction and given the nature of the international economic environment merit that, and I think it's very important that this role within the Treasury be perceived in those terms.

Second, while I understand that the nomination was referred to the Finance Committee and reported out by it, and I certainly support a favorable report on this nomination, I think it's important that this committee have this opportunity to have the nominee before it on the range of issues that are involved, because many of them are in fact direct responsibilities of the Banking Committee.

In fact, the provisions in the trade bill last year, the titles, many of the titles that this committee handled that are now in the trade bill, are very directly related to the responsibilities that Under Secretary Mulford will have to carry out. For examle, the international exchange provisions, the debt provisions.

First of all, we require a report twice a year on the exchange rate policy, international economic and exchange rate policy, and in fact the Secretary and the Under Secretary were here just last week, testifying on that matter and will be back before us once again in 6 months time for such a report.

Second, last year, we held extensive hearings in the subcommittee on the debt question, and the administration's report was submitted to us earlier this year in response to the mandate given in the trade bill. So I think it's very important that the Banking Committee, through this hearing and in other ways, establish a very close relationship with the Under Secretary.

It is in fact the case that under the terms of the law, many of your reports come directly to this committee, is it not?

Mr. MULFORD. Yes, that's right. Yes.

Senator SARBANES. So a good deal of your time actually in terms of preparing for and testifying to the Congress directly relates to this committee.

Mr. MULFORD. That's right, yes.

Senator SARBANES. Well, Mr. Chairman, I wish that I could stay. Unfortunately, I can't But I did want to establish that record and I do very strongly commend this nomination. I look forward to being supportive of it on the floor. I don't anticipate any difficulties with it, and we look forward to Secretary Mulford continuing to carry forward on his responsibilities.

Let me just add one thing. I understand there is a notion floating around of—as you address the debt issue, I think the assurances that are being talked about, provided by the international institu-

tions to the banks, should more closely relate to existing debt, either a draw-down on its principal and then how you handle the remainder, or an easing of the interest burden, rather than new money.

I know there's a proposal floating around apparently. But that seems to me a very open-ended proposition, and I think it should be looked at very carefully.

I don't know if you have any reaction to that.

Mr. MULFORD. Well, I do. I think that's right. The proposals that we made in the international institutions have to do with the provision of support for transactions that have the effect of reducing the stock of debt or reducing interest. We have not, although we have stressed the importance of new money from the banks, we have not made proposals to provide enhancements from the international institutions to the banks for new money. That's quite clear. And that misunderstanding should be cleared up.

Senator SARBANES. But that, if undertaken, could be a very open-ended proposition. Second, it seems to me that the judgment on the provision of new money would be made in the context of whatever assurances were provided, and the results thereof, with the treatment of existing debt principal or existing interest costs.

Mr. MULFORD. The thrust of the idea is wrong because you would be enhancing the creation of new debt and therefore emphasizing an increasing stock of debt. And there would be strong opposition to these ideas from others besides the United States within the group of major creditor countries.

Senator SARBANES. Thank you very much.

The CHAIRMAN. Senator Sarbanes, I appreciate your warm comments in support of this nomination.

Senator SARBANES. Mr. Chairman, I have to confess that I discovered Secretary Mulford's Oxford education well after or subsequent to developing a respect for his abilities and some of his leadership on these issues. So I want to be very clear that it did not precede, but in fact it followed.

The CHAIRMAN. I see.

Senator Wirth, let me indicate that Under Secretary Mulford is going to be testifying before the Finance Committee at 10:00 this morning. I would like to yield to you at this time so that you can have a question period, and then I have a few more items that I want to cover before we finish.

Senator WIRTH. Thank you, Mr. Chairman.

Mr. Secretary, welcome. I am pleased to see you here. We had the opportunity of serving together as White House Fellows some 20 years ago. And it's nice to have you here and serving the country in such an able way.

I have a couple of questions, if I might. The first one perhaps is best summarized by a couple of recent press reports, maybe you would like to comment on these, in The American Banker of the 5th of May. Quote:

> The Bank of England warned Thursday that proposals by U.S. Secretary Brady for reducing the Third World debt had raised unrealistic expectations among debtor nations.

Two days before, the Wall Street Journal said:

The Bush Administration's new debt strategy which emphasizes debt reduction over continued lending, is meant to improve U.S. relations with Latin America. Instead, it is causing frustration and concern in the region.

I understand, also from individuals who are deeply involved with Mexico, that there were again a number of expectations raised about this, Secretary Mulford, and people feeling very frustrated that after the initial rush of enthusiasm, very little has been done.

What is your response to, one, these criticisms—because that's what they are. And, second, what about steps the administration is going to be taking?

Mr. MULFORD. I would make several comments about that. First of all, before the proposals were announced, we had a situation in which there were declining expectations, debt fatigue (so-called), demoralization, a lack of hope, and so on.

Since the proposals have been made, we are now hearing that there is a rise in expectations and that this is excessive.

My own view is very simple on this matter. It is far better to have expectations on the rise and to understand that when that happens, there will have to be a period, since this is a negotiating process, during which those expectations on both sides of the negotiating table have gradually to be defined into realities. This will take a little time.

And that brings me to my second point; that in a process as complex as this, and with so many moving pieces that have to be fit together, and with the new policies that have been proposed with rather a lot of technical details that have to be worked out among the institutions, the commercial banks, and so on, you're inevitably going to have a period of uncertainty. That is the sort of thing we are seeing at the moment.

But again, this is inevitable if you're going to make a major change. And since we have all agreed that a major change is necessary—and by "we," I mean all of the various players did agree and were very supportive in their beginning comments about the general change in direction—we have to accept, it seems to me, some process of living with expectations and dealing with the uncertainties.

In the end, I would say that we now have a situation which has more hope, more momentum—the various parties are engaged in constructive negotiations and the institutions are engaged in positive discussions to make important changes in policies.

So, personally, I see this as a very positive process despite these obvious problems.

Senator WIRTH. I hope you're right. The reason for bringing it up was just to underscore the concerns that I think many people, not only up here but in the economic community around the country, feel for the rapidly deteriorating economic situation, particularly in Latin America. The perceived and real debt overhang, the political problems that come along with that, and the potential gap between the United States, our interests, and the rest of the hemisphere are all issues for concern.

This, it seems to me, is probably as important a wedge as we have. You know that, but I think the urgency that is felt in countries in South America—the urgency which many people feel as the European community comes together in 1992, many perceive

that we are going to be shut out as part of that community, that our natural community going north-south is being neglected.

It seems to me there are a variety of variables coming into this that would suggest that perhaps the termperature ought to be raised significantly in these negotiations. Mexico is the lead, as you have ponted out and as we all know. It's a very, very important negotiation. If frustration is felt in Mexico, imagine what the Brazilians are thinking or the Argentineans are thinking.

Mr. MULFORD. The points you made about Latin America are exactly the reasons why we made the changes that we've made in the strategy and why we're moving now with some speed to implement those.

Senator WIRTH. I think it's a question of a sense of urgency, and I think that that frustration is showing there, and I suspect it's going to start showing up here.

Let me jump, if I might, to the second issue I wanted to raise with you. On the 30th of March, Senator Heinz and I wrote a letter to Secretary Brady about the Brady Plan and the relationships of the Plan to the environment. We have not heard anything back, which I though was surprising, given discussions that we've had, and I would hope that maybe you could go back and talk to people in Treasury. Again, if there's a sense of urgency, 7 weeks out from a letter from two members of the Banking Committee I think is a bit surprising.

The thrust of the letter, let me just quote a couple of points from it:

> There is growing recognition that debt and environmental conditions in developing countries are inextricably linked.

We then go on to suggest four areas that we ought to be looking at: first, policies and incentives to encourage and channel new loans to support projects that make both economic and environmental sense; second, debt reduction packages to encourage progressive changes in debtor nations related to the environment; third, that the United States should pick up on the very good work that you all did in your Report to Congress on Debt for Nature Swaps; and finally, urging that the United States take the lead with the G–7 countries in looking at the potential of debt for nature swaps.

What strikes me and, I will tell you, disappoints me, I have been very involved with the discussions with the current Administration on their initiatives on global warming, and you've read all of the very unfortunate press that the Administration received in the last week about its apparent inability to engage this issue of global warming, which is about as obvious as they come.

Another major issue coming down the line is the potential of debt for nature swaps. On the one hand, we're talking to the Administration about the global warming question and getting back an OMB effort to change testimony by scientific experts. On the other hand, Senator Heinz and I wrote, 6 weeks ago, what I thought was a very thoughtful and sort of hopeful letter; haven't heard a word. And we get from the World Bank and from the Inter-American Development Bank that they don't believe that our

Treasury really takes this set of environmental concerns very seriously.

So I am going to lay that out, David. You all have got a whole new set of arrangements and new set of issues. I'm only saying that I think there's possibility here that you are significantly missing, or may be significantly missing an enormously important agenda, and I raise this only for any attempt to perhaps get it up your scale a little bit, maybe get up from a 1 to a 2—I would hope it would be closer to a 10—but just to move it up a little bit more than it has been so far.

Mr. MULFORD. I would first of all apologize for the fact that we haven't responded. I'll check into that right away. We should have done. Seven weeks is too long.

Second, I am very sympathetic to the points you have made. That is a very personal agenda. I would give you my personal undertaking that the Treasury does take seriously these issues you've mentioned, including debt for development swaps, debt for nature swaps. We've done a lot of work on those to bring those along.

Regarding the environmental issues and the environmental sensitivity of the MDB's and the IDB, for example, under the replenishment just negotiated in March, there is a new environmental unit being established of the World Bank. So I can give you a personal assurance it will be much higher than a 2 on my agenda.

Senator WIRTH. Well, you did a very good piece of work on the Treasury Report last year. I mean that is really helpful, but where is it being used? Has somebody talked to Mr. Conable about that to Mr. Iglesius?

Mr. MULFORD. Yes.

Senator WIRTH. They are all looking to us for leadership. We've met with them and don't get a sense that there is a coherent concern about this, and maybe you can help to raise that.

Mr. MULFORD. In Amsterdam, during the IDB negotiations, I personally took the matter up with Mr. Iglesius and each of the Latin Finance Ministers, and underlined it's important to us in the replenishment and so on.

Senator WIRTH. Great. Good luck. We're glad that you are taking on this job. I'm proud to have you there and look forward to working with you.

Mr. MULFORD. Thank you very much.

The CHAIRMAN. Before going to Senator Pressler, I want to touch on a couple of others items. I know we're pressed against the 10 o'clock hour here. Going back to the Citibank action on the Ecuadoran assets, did they notify you ahead of time that they were going to take this action?

Mr. MULFORD. No, they did not.

The CHAIRMAN. So how did you find out about it?

Mr. MULFORD. I can't remember whether we heard first from Ecuador or from Citibank after the fact, but we heard pretty quickly from both sides afterwards.

The CHAIRMAN. Were you surprised that you didn't get any advanced notice that this was about to happen?

Mr. MULFORD. I suppose, in retrospect, somewhat surprised.

The CHAIRMAN. I would assume that in the normal course of events, you are in conversation with the major banks that hold

most of the Third World debt. My own impression, from arm's length, would have been that if they were planning a major action of that kind—which I take this to be—that as long as they're a party to other discussions and efforts by the Government, that as a matter of course you would be alerted to that.

Mr. MULFORD. Well, my impression is that within Citibank, this was regarded as more of a legal issue than a commercial issue. That perhaps explains why the people one is normally in touch with on the commercial side on these debt issues didn't mention it.

However, I do think it is significant that the Ecuadorans were in discussion with the banks about beginning to make payments on their arrears and had, we understand from them, made certain undertakings that they would do this when this event took place.

The CHAIRMAN. Has it set off secondary shock waves with respect to other countries now that come to you on this issue?

Mr. MULFORD. We have not heard from other countries at this time.

The CHAIRMAN. Well, I want to raise one other issue and then I want to yield to Senator Pressler. We have looked over the financial reporting forms, as we do for all the candidates, and we observed in doing so that you've got holdings in a number of firms that have international business dealings. Not surprising. Almost every business today does.

Mr. Glauber, who is going to come after you this morning, like many others, has chosen to put his holdings in a blind trust. He also has a long list of holdings.

Are you intending to create a similar kind of blind trust arrangement?

Mr. MULFORD. Well, I will do whatever I am advised to do by the General Counsel of the Treasury and also the Ethics people in the White House.

I would like, for your clarification though, Mr. Chairman, to point out that—and I am not a specialist in these matters, I just try to do the best job I can in making sure that these are handled properly—when I arrived in Washington the first time, I was advised that I should create a trust. I did so at considerable time and expense to myself.

Very shortly thereafter, something like 18 months, I think there was a change in people, and I was advised that I should not have a trust. I expressed by personal view at that time, that I would like to have the trust purely for the political protection that I felt that would give me, but I was strongly advised to undo the trust.

I therefore undid the trust and have recused myself on the advice of the General Counsel of the Treasury from those areas that seem to have a potential conflict, one of which is VRA's, for example, steel VRA's. And I will continue to take the advice of the General Counsel of the Treasury and the Ethics people and do whatever they feel I should do.

I would like to be spared too much of this back and forth business, however.

The CHAIRMAN. I take it that the Bush Administration has established for itself some new standards, different standards. There have been a number of instances, as you know. In any event, I take

it that that issue isn't fully resolved, then, one way or the other at this point.

Mr. MULFORD. It has been discussed in recent times, and the impression I have is that I should not have a trust. I don't fully understand the reasons for that, since I personally would be quite happy to have one, but I am sure we will continue to discuss it and they will give me ultimately the final advice that I need on that.

The CHAIRMAN. All right. And perhaps we can talk about it as well after this hearing.

Mr. MULFORD. Certainly.

The CHAIRMAN. Senator Pressler, let me yield to you at this point.

Senator PRESSLER. Thank you very much and welcome. I think we have before us a person who is very knowledgeable in your areas.

Let me ask you about the debt situation with Paraguay. Is that something you have followed closely?

Mr. MULFORD. It is really not a situation I have followed closely. I have, in fact, relatively small knowledge of it.

Senator PRESSLER. Is that because there are less problems with Paraguay and debt, both with private banks and public institutions?

Mr. MULFORD. Paraguay, as I remember, has a relatively small amount of commercial bank debt, and prior to the change in government there, personally speaking, I had virtuallky no contact with them.

Senator PRESSLER. I'm supposed to go down there this weekend to the inauguration of the new president, or to the change of government. And I'm going to try to brief myself on that subject.

Let me ask you, on this Citibank situation, according to The Post, it said that the loans are subject to so-called sharing clauses which specify that if one bank succeeds in extracting money from a recalcitrant debtor, it must share the proceeds with the other banks that are party to the loan.

Is that a usual practice?

Mr. MULFORD. That is a usual provision in all the international lending agreements, in the syndicates that banks form, so that when any money is received, it is shared pro rata according to the exposure of the banks among the banking community.

Senator PRESSLER. Do you suppose the Citibank did this maybe as a signal to other countries that are also in debt to Citibank?

Mr. MULFORD. I don't know the answer to that. I would say on the sharing provision question, that on this case this was outside the sharing provision, it was a trade facility arrangement, and therefore it is Citibank alone that is acting and Citibank that will take the $80 million.

Senator PRESSLER. Let me say on the face of it, I don't see a problem. If somebody, if they owe Citibank a substantial amount of money, and depending on what their agreement was, I don't fully understand the situation. But do you see any problem with what Citibank has done?

Mr. MULFORD. I said earlier when I was asked that question that Citibank certainly is within its legal rights to take that action. The fact that Ecuador has allowed its arrears to go untended for a long

period of time and to rise to very high levels has contributed to the situation, but I also expressed the personal view that I thought the action was perhaps politically insensitive.

Senator PRESSLER. Thank you very much.

The CHAIRMAN. Thank you, Senator Pressler.

Mr. Mulford, just a couple of other items here that I think it's important for us to cover today. You state on page 4 of your testimony that you have continuing responsibility within the Treasury Department for investment issues.

The Congress enacted provisions dealing with foreign investment in the Omnibus Trade Bill, and they are contained in Title VII of the Defense Production Act, which is under this committee's jurisdiction.

Did the President assign the chief responsibility for the review of foreign investment contained in that title to the Treasury Department?

Mr. MULFORD. Yes.

The CHAIRMAN. Are the Treasury Department officials who carry out these responsibilities under your supervision?

Mr. MULFORD. Yes.

The CHAIRMAN. Can you tell me who the principal people would be that are involved in this work? I'm thinking of job title as much as name.

Mr. MULFORD. The Deputy Assistant Secretary for Trade and Investment, Mr. William Berrada, and his Office Director, Mr. Steven Canner, are the two principal participants, together with, of course, the legal people in Treasury's General Counsel Office. And then myself, I chair the committee that meets on those matters.

The CHAIRMAN. Can you give a sense as to the share of time that might go to the investment issues?

Mr. MULFORD. Oh, that rises and falls. Sometimes it's very small, and suddenly there will be a run of issues. But I would say probably 2 or 3 percent.

The CHAIRMAN. Finally, one other question. Section 3602 of the Omnibus Trade Bill gives the Secretary of the Treasury the lead responsibility to negotiate to ensure that U.S. financial institutions receive national treatment in their operations abroad. The Secretary is to report to the Congress by December 1st of 1990 on the success of such negotiations.

Is that area of the Treasury Department's duties under your supervision?

Mr. MULFORD. Yes, it is.

The CHAIRMAN. I take it that that's an area that will be of some priority, particularly because the European community is moving to Europe 1992. Is that accurate?

Mr. MULFORD. That's correct. High priority.

The CHAIRMAN. Can you give me a sense as to the percentage of time that is likely to be devoted to that area?

Mr. MULFORD. Well, since I arrived at the Treasury, that flows with the need to prepare Treasury's periodic report on national treatment. So we go through long periods where I spend almost no time, and then I'll spend a modest amount of time. However, it's growing now and I would put it at the moment at probably 2 percent.

The CHAIRMAN. Very good.

I want to thank you for your appearance this morning and for the directness of your answers. We look forward to working with you and I may have another question or two for the record that I'd ask you to respond to.

Mr. MULFORD. Thank you very much, Mr. Chairman. I appreciate being here.

The CHAIRMAN. Thank you. Let me excuse you now and let you make the trip down to the Finance Committee.

Mr. MULFORD. Thank you.

[Whereupon, at 10 a.m., the committee proceeded to other business.]

[Appendix follows:]

APPENDIX

Summary of Legislative Proposals

The following measures were proposed by the SEC and were introduced in the Senate on March 17, 1989 at the request of the agency. It is expected that at the April 18th hearing, SEC Chairman Ruder will testify on the need for each of these measures.

A number of these bills are controversial and will require additional hearings in the future, at which investor and business representatives, as well as other commentators, will testify. A more detailed discussion of the legislation together with the text of the bills may be found in the March 17, 1989 Congressional Record, pages S 3038 - 3054; S 3064 - 3068.

S.646 THE INTERNATIONAL SECURITIES ENFORCEMENT COOPERATION ACT OF 1989

This bill is designed to strengthen international cooperation in the enforcement of securities laws, so that U.S. investors will continue to be afforded the protection of our laws in an increasingly global trading environment. A nearly identical measure(except for two provisions noted below), S.2544, was introduced in the last Congress and was unanimously reported out of the Committee last July.

The legislation would further international cooperation among securities regulators by giving the Commission the authority to maintain the confidentiality of certain foreign evidence. The Commission has expressed concern that, in the past, negotiations of bilateral assistance agreements have been frustrated by the agency's inability to assure foreign authorities that documents and testimony they transmit to the Commission will be kept confidential, as is often required under their resident laws. The Commission currently has disclosure obligations under the Freedom of Information Act and pursuant to third party subpoenas. This legislation would exempt documents furnished to the Commission from disclosure if the foreign authority represents that the disclosure of the documents would violate confidentiality requirements of its country's laws.

The bill also would make explicit the Commission's rulemaking authority to provide documents and other information to foreign and domestic authorities.

In addition, the bill would amend the Exchange Act, the Investment Advisers Act, and the Investment Company Act to authorize the Commission, based upon the findings of a foreign court or foreign securities authority, to censure, revoke the registration of or impose employment restrictions upon securities professionals registered to do securities business in the United States. The Commission already has this authority as to illegal

or improper activity in this country, and it has imposed limitations on activities of securities professionals based upon the findings of a foreign court as to certain illegal activity abroad. This bill would make this authority explicit, and would add to the Commission's authority as well. The legislation would give the Commission authority to suspend or bar securities professionals who have made false filings with foreign authorities; who have been convicted of certain crimes by foreign courts(addition to S.2544); who have been enjoined by a foreign court from committing securities law violations; who have violated foreign securities laws; or who have aided and abetted such violations.

The legislation also would expand the grounds on which a self-regulatory organization could deny a person membership in, participation in, or association with a member of, the SRO. It would permit the Commission and the SROs to provide special scrutiny of persons who have been convicted of crimes that currently are not specified as grounds for denying a person membership, participation, or association with an SRO, such as drug trafficking, assault and other crimes.

The bill also would permit the Commission to accept reimbursement from a foreign securities authority for travel and other expenses incurred by the Commission in carrying out investigations for that foreign authority(addition to S.2544).

S.647 THE SECURITIES LAW ENFORCEMENT REMEDIES ACT OF 1989

This bill is designed to strengthen the enforcement capabilities of the Securities and Exchange Commission and enable the Commission to tailor enforcement remedies more appropriate for particular facts and defendants.

This legislation in large measure builds upon the philosophy underlying the Insider Trading Sanctions Act and subsequent amendments to that Act, which gave the Commission authority to seek civil penalties for insider trading violations. The bill would authorize the Commission to request that federal courts impose civil penalties for certain other violations of the federal securities laws. In addition, it would authorize the Commission to impose civil penalties in certain administrative proceedings under the Securities Exchange Act of 1934, the Investment Company Act of 1940, and the Investment Advisers Act of 1940.

In addition to the civil penalty provisions, the proposal contains three other new enforcement remedies. It contains express authority to provide that federal courts can, as ancillary relief in Commission injunctive actions, prohibit an individual from serving as an officer or director of any reporting company. It would permit the Commission to impose such

a prohibition in its administrative proceedings under Section 15(c)(4) of the Exchange Act, and it would give the SEC authority to bring administrative proceedings against officers and directors and principal stockholders for violations of the reporting provisions of Section 16(a) of the Exchange Act.

In its memorandum in support of the legislation, the Commission stated that the legislation was based in large part upon the Commission's response to certain recommendations of the National Commission on Fraudulent Financial Reporting, known as the "Treadway Commission." In addition, the Insider Trading and Securities Fraud Enforcement Act of 1988 directed the Commission to submit to Congress recommendations with respect to civil penalties and administrative fines.

The Commission has urged Congress to adopt this legislation on the basis that the additional sanctioning authority will enable the Commission to tailor enforcement remedies more precisely to particular facts, and thereby to maximize the effectiveness of its enforcement actions. In addition, the Commission has said the creation of more severe penalties would inject a greater general deterrence aspect into its enforcement program. The Commission currently does not have the flexibility in seeking or imposing civil money damages that several of the self-regulatory organization have. Finally, the Commission has urged that, by giving it express authority to impose corporate bars and suspensions, the legislation would resolve any doubts about the propriety of this remedy, which has been obtained in Commission injunctive actions by consent.

S.648 THE MARKET REFORM ACT OF 1989

This bill is designed to address potential gaps and weaknesses in current market regulation and market practices identified in studies by the Securities and Exchange Commission and others following the October 1987 market crash. The legislation was submitted to Congress by the Commission on June 23, 1988, as four separate provisions.

The four measures have been combined for the purpose of introduction as "The Market Reform Act of 1989."

Emergency Authority/Trading Halts. The legislation would provide the Commission with authority to take temporary emergency action without procedural delay in response to a major market disturbance. This authority would include, but not be limited to, the ability to alter, supplement, suspend, or impose requirements or restrictions with respect to hours of trading, position limits and clearance and settlement. This emergency authority could be exercised if there were a substantial threat of sudden and excessive fluctuations of securities prices generally that would threaten fair and orderly markets, or a

substantial disruption of the safe or efficient operation of the national system for clearance and settlement of securities. The Commission's action taken under this legislation would be subject to judicial review.

Large Trader Reporting. The legislation also would provide the Commission with authority to adopt reporting rules relating to large securities transactions and certain transactions in the futures markets that are related to transactions in the securities market. In its memorandum supporting the legislation, the Commission noted that this section is modeled after the large trader reporting authority of the CFTC. It is designed to assist the Commission in its surveillance of the U.S. securities markets by providing it with broad authority to adopt reporting rules for the purpose of monitoring the impact on the securities markets of large transactions in publicly traded securities involving a substantial volume or a large market value in equity index futures and options on such futures. The Commission could use information contained in the reports for surveillance, enforcement and other regulatory purposes.

Risk Assessment for Holding Company Systems. The legislation would expressly authorize the Commission to require certain entities registered with the Commission, including brokers and dealers, to report information relating to their associated persons that may have a material impact on the financial or operational condition of the registered entity. Under this legislation, the Commission could adopt rules requiring information concerning, among other things, assets, liabilities, contingent liabilities, material contracts, loan commitments, trading or investment positions, lines of credit, letters of credit, and financial guarantees. However, where information regarding the activities of banks, insurance companies, futures commission merchants and other regulated institutions is available to another supervisory agency, information would not be required under this provision. Moreover, the Commission would have exemptive authority.

Coordinated Clearing. The legislation would direct the Commission and the Commodity Futures Trading Commission, in consultation with the Board of Governors of the Federal Reserve System, to facilitate the establishment of linked, coordinated, or centralized facilities for clearance and settlement.

In its memorandum in support of the legislation, the Commission observed that the clearing systems for securities, securities options, futures contracts and options on futures, and commodity options affect the nation's financial systems. The clearing procedures employed for these products potentially can affect, through settlement default or lack of coordination with other clearing systems, other cleared products, clearing systems, and financial systems.

S.649 SHAREHOLDER COMMUNICATIONS IMPROVEMENT ACT OF 1989

This bill is designed to improve the flow of information to mutual fund and other investment company shareholders.

The legislation would extend to mutual fund and other investment company security holders the benefits of the Commission's shareholder communication rules which now require brokers and dealers, banks, associations, and other entities that exercise fiduciary powers holding securities in nominee name to deliver proxy materials to the beneficial owners and to supply registrants, upon request, with beneficial owner information so that they can send annual reports and voluntary communications directly to beneficial owners.

It also would require broker and bank nominees to transmit information statements to the beneficial owners of the securities. In addition, beneficial owners of investment company securities also will be included among those security holders to whom nominees must deliver information statements.

S.651 TRUST INDENTURE REFORM ACT OF 1989

This bill is designed to streamline and improve the disclosure requirements for the issuance of debt securities and enhance the protection of security holders. The legislation was first submitted to Congress by the SEC on November 17, 1987, and it was introduced at the request of the agency by Senators Proxmire and Garn on June 24th of last year.

The Commission developed this legislation for the purpose of modernizing the Trust Indenture Act of 1939, which currently regulates the public issuance of debt securities and the relationships among security holders, the indenture trustee and the obligor. Since the adoption of the current law, there have been significant changes in the markets, with respect to both the types of debt securities offered to the public and the techniques for their sale. As a result, the Commission has advised Congress that aspects of the Act have become administratively or substantively obsolete.

The Commission has further stated that this legislation would modernize the law while continuing to mandate necessary protections for debt holders. For example, while current law requires that indentures set forth certain mandatory requirements, this legislation would make those requirements self-executing by law, those avoiding unnecessary "boilerplate" language in disclosure documents.

The legislation would also give the Commission greater exemptive authority in order to permit the Commission to adjust requirements to particular needs when their application would impose undue restrictions and would be unnecessary to serve the purposes of the law. The legislation would make further revisions in the conflict of interest provisions of current law, as well as revisions affecting the qualifications of foreign trustees.

NOMINATION OF ROBERT R. GLAUBER, OF MASSACHUSETTS, TO BE UNDER SECRETARY FOR FINANCE OF THE DEPARTMENT OF THE TREASURY

FRIDAY, MAY 12, 1989

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The committee met at 10:01 a.m., in room SD-538 of the Dirksen Senate Office Building, Senator Donald W. Riegle (chairman of the subcommittee) presiding.

Present: Senators Riegle, Dixon and Wirth.

OPENING STATEMENT OF CHAIRMAN RIEGLE

The CHAIRMAN. Mr. Glauber, let me welcome you to the committee this morning. You are a familiar face and we are delighted to have you appear before us today. You have, of course, been involved already in a number of key responsibilities which have been exercised within the Bush Administration, specifically related to the savings and loan rescue plan and that legislative package.

You will also have major responsibilities in Treasury for policies that deal with capital and securities markets—I want to get into that in a bit—financial institution modernization, and the financial aspects of corporations, including leveraged buyouts. Each of these issues has been and will continue to be of intense and direct legislative interest to this committee and clearly falls within the jurisdiction of the committee.

I made a comment earlier this morning with respect to the background of this hearing and the hearing with Mr. Mulford. I won't repeat all that's in the record. But serving as I do, as a member of the Senate Finance Committee, as two other colleagues of this committee do, Senator Heinz and Senator Roth, while the Finance Committee historically has had the confirmation responsibility, there is a clear overlap of jurisdictional legislative work that goes back and forth between the two committees. And I want to again express my appreciation to Senator Bentsen for his courtesy and comity in working with us so that we would have this opportunity to hear from you and Mr. Mulford prior to the time these nominations went on to the Senate floor.

So we will look forward not just to our discussion this morning, but to the opportunity to work together on a number of issues

going ahead in time, as we have already been able to do with respect to the savings and loan issue.

Now, throughout the remainder of the 101st Congress and for this foreseeable future, the Senate Banking Committee expects to devote a majority of its time to three issues. savings and loan industry issues, financial modernization, and market reform. Now, there are a host of other issues that might be mentioned, but these are three major issues that are before us.

I have a number of brief questions in each of these areas and I would just ask you for an appropriate but not necessarily overly long response, unless you feel the need to give one.

Before I do that, I want to give you an opportunity to make any initial comment that you would like to make. We would be interested in having you do that and to give perhaps a brief summary of your professional background leading up to this very important assignment.

STATEMENT OF ROBERT R. GLAUBER, NOMINEE TO BE UNDER SECRETARY FOR FINANCE OF THE DEPARTMENT OF THE TREASURY

Mr. GLAUBER. Thank you very much, Mr. Chairman. I have a somewhat longer statement which, if I could, I would like put in the record——

The CHAIRMAN. Without objection.

Mr. GLAUBER [continuing]. And, if I may, just read a very brief summary of that longer statement.

Mr. Chairman, I have the honor of being nominated by the President for the position of Under Secretary for Finance of the U.S. Treasury. It is also an honor to appear before this committee.

The responsibilities of my position include the offices of Domestic Finance, Economic Policy, and Fiscal Management. Domestic Finance has primary responsibility for developing policies to deal with the capital and securities markets, financial institutions, and financial aspects of corporations.

Economic Policy acts as economic advisor to the Secretary of the Treasury, participates in producing the Administration's economic forecast, and provides staff support on economic issues. These issues include the savings rate, retirement policy, and, together with the Office of Tax Policy, the impact of tax policy on corporate decisions.

Fiscal Management acts as the Government's fiscal and financial manager, handling Federal collections and payments and collections and overseeing its central accounting and reporting systems.

I believe my experience as a teacher and researcher on finance issues at the Harvard Business School, as a consultant to financial institutions and business corporations, and as Executive Director of the Presidential Task Force empaneled to study the 1987 stock market break provides useful preparation for the duties for which I have been nominated.

I would like to discuss very briefly three policy issues: leveraged buyouts, financial institutions and securities markets, in which the rapid internationalization of competition is strongly affecting U.S. financial corporations, institutions, and markets.

In the area of leveraged buyouts, I think the question to ask is: Is the rising trend of LBO's a healthy one for U.S. corporations? In my view, judgment should be based primarily on whether or not LBO's contribute to the competitive position of U.S. corporations.

The evidence on LBO's is ambiguous and incomplete. In addition, there are difficulties with some of the suggested solutions. Making dividends tax deductible, to reduce tax incentives to replace equity with debt would be hard to achieve, given the current size of the fiscal deficit.

Eliminating the tax deduction for some or all interest payments would raise the cost of capital for U.S. corporations in favor of foreign companies, using tax-deductible debt in acquisition attempts. Moreover, trying to define what debt or equity is, or what excessive leverage is, is a far from simple matter.

Accordingly, legislative initiatives at this stage should be limited, in my view, although some steps proposed by the Administration would be useful to implement now: capital gains tax reductions to encourage long-term investment decisions and clarification of the ERISA laws to indicate that pension fund trustees are not obligated to take a bit higher than current market price from fear of litigation.

In the area of financial institutions, the position of U.S. financial institutions in the international arena has been declining over the last decade. For U.S. banks, several forces are at work, including the change in exchange rates and a more concentrated structure of banking abroad as compared with the United States. But the restricted rate of activities permitted to U.S. banks also has played a role. The broadening of such activities would enhance the competitive position of U.S. banks by stabilizing and increasing their profitability, and it would allow U.S. banks to meet their foreign competitors on a more level playing field, since certain foreign banks can engage in activities in the U.S. prohibited to the U.S. competitors.

As the financial services industry continues to evolve, the distinction between commercial banks and thrifts may become less one of economics than market focus. That is, there may be more in common among most thrifts and a great majority of banks, all directed towards serving community retail financial needs, than between these banks and their multinational counterparts whose major focus is on the wholesale banking needs of corporations and similar institutions.

If this occurs, development of legislation on such issues as permitted banking activities and deposit insurance will likely be simplified.

Finally, in the area of securities markets, the October 1987 market break revealed important weaknesses in both the institutional structure and regulation of these markets. Competition among the marketplaces for stocks options and financial futures is essential to continued capital market innovation in the face of increased pressure of global competition.

But to operate efficiently and safely, these separate marketplaces must be part of a system which reflects, both in institutional structure and regulation, the economic functioning of one market.

As we press our efforts to resolve our own intramural disputes between New York and Chicago, between the SEC and the CFTC, we should keep our eye on the longer goal of protecting and extending the economic leadership of our markets in the arena of the international capital markets. Unlike the auto industry, information requires no factories. Leadership can be lost quickly and, once lost, is not easy to regain.

Over the last year, positive developments have occurred to enhance the integrity of the one-market system; for example, in circuit breaker mechanisms and in cross- margining discussions. And those were initiatives of the private organizations themselves. Yet little has been done to coordinate and integrate the clearing and settlement systems of these marketplaces, so necessary to assure that the U.S. market relates effectively to one another and are integrated into the evolving global clearance and settlement system. This should be a major goal of the Working Group on Financial Markets.

Thank you very much. I would be most happy to answer any questions you or the committee might have.

[The complete statement of Robert R. Glauber follows:]

FOR RELEASE ON DELIVERY
EXPECTED AT 10:00 A.M.
FRIDAY, MAY 12, 1989

STATEMENT OF
ROBERT R. GLAUBER
NOMINEE FOR UNDER SECRETARY (FINANCE)
UNITED STATES DEPARTMENT OF THE TREASURY
BEFORE THE COMMITTEE ON
BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE

Mr. Chairman, Senator Garn, distinguished members of the Banking Committee, I have the honor of being nominated by the President for the position of Under Secretary for Finance of the U.S. Treasury. It is also an honor to appear before this Committee.

The responsibilities of my position include the Offices of Domestic Finance, Economic Policy, and Fiscal Management. Domestic Finance has primary responsibility for developing policies to deal with the capital and securities markets, financial institutions, and financial aspects of corporations. Economic Policy acts as economic advisor to the Secretary of the Treasury, participates in producing the Administration's economic forecast, and provides primary staff support on economic issues. These issues include the savings rate, retirement policy, and (together with the Office of Tax Policy) the impact of tax policy on corporate decisions. Fiscal Management acts as the government's financial manager, handling federal collections and payments and overseeing its central accounting and reporting systems.

I believe my experience as a teacher and researcher on finance issues at the Harvard Business School, as a consultant to financial institutions and business corporations, and as Executive Director of the Presidential Task Force empaneled to study the 1987 stock market break provides useful preparation for the duties for which I have been nominated.

I would like to take just a few minutes to outline some of the major policy issues with which I would deal if confirmed, apart from the current thrift crisis.

International Competitiveness

It is perhaps stating the obvious to point out that the rapid internationalisation of competition is one of the strongest forces confronting U.S. corporations, financial institutions and financial markets. If these institutions are to maintain and extend their competitive position and economic leadership, we must frame policies which take explicit account of these goals and give due consideration to the international arena in which these institutions must compete. As you know, the Secretary in a number of statements has directed attention to these concerns and intends to play an active role.

A. Leveraged Buyouts

At the beginning of this legislative session, Congressional Committees held hearings on leveraged buyouts (LBOs), an issue which has important implications for the competitiveness of U.S. corporations. Contrary to forecasts that the 1986 tax rate reductions would sharply reduce the LBO business, the amount of such transactions has been rising. Is this trend a healthy one for U.S. corporations? In my view, judgement should be based primarily on whether or not LBOs contribute to the competitive position of U.S. corporations.

The arguments are many and are arrayed on both sides. On the positive side: management works harder when it owns a significant piece of the equity, high debt levels can act as an effective discipline on management, and private firms are not subject to the short-term performance demands of the stock market.

At the same time there are aspects of LBOs which are a basis for concern. First, more transactions are being done for companies in cyclical industries--chemicals, paper, etc. When the economy finally slows down, what will happen to these firms, not just their bondholders and stockholders, but also their workers and the communities in which the firms operate? Second, under pressure to service debt, heavily leveraged companies may cut back on R&D and capital expenditures--in short, they may become more short-term oriented when private than they were as public firms. Third, the level of LBO debt held by insured banks is growing, leading some to question whether sufficient due diligence has been performed. Finally, many of the brightest people coming out of college and business schools are spending more time recapitalizing old firms rather than rebuilding them or creating new ones.

The evidence on LBOs is ambiguous and incomplete. While aggregate debt levels are not beyond historical bounds, levels in certain industries and specific transactions can be cause for concern. Moreover, the recent LBO trend has gone on against a background of healthy economic expansion; how well will these

highly leveraged firms perform in a period of economic decline, where past history cannot be the guide?

My view is that any legislative initiatives at this stage should be limited, reflecting the inconclusive nature of the evidence. Some steps proposed by the Administration, though, would be useful to implement now--capital gains tax reductions, to encourage long-term investment decisions, and clarification of the ERISA laws, to indicate that pension fund trustees are not obligated to take a bid higher than current market price from fear of litigation.

A more sweeping and potentially more effective proposal would be to make dividends tax deductible, so that companies do not have tax incentives to replace equity with debt. The tax codes of virtually all other major industrial countries exempt dividends in whole or in part. But given the current size of the federal budget deficit, such a revenue reduction would be difficult to achieve.

The elimination of the tax deduction for some or all interest payments is an equally sweeping legislative initiative but, in my view, is overreaching. It would adversely affect the competitive position of U.S. corporations, by raising their cost of capital and by favoring foreign companies, which can use tax-deductible debt, in acquisition battles. Moreover, any attempt to eliminate the deduction for "bad" debt--for example, debt involved in "hostile" takeovers or raised by "excessively" leveraged firms--has and would produce definitional and administrative nightmares.

B. Financial Institutions

Several recent legislation initiatives have important implications for the competitive position of U.S. financial institutions. The secular decline in the profitability of these firms during the 1980's--commercial banks as well as thrifts--can be traced in some considerable measure to the competition from insolvent S&Ls which have been permitted to remain in operation. Continuing to compete in the marketplace, these institutions have pushed up deposit costs and reduced profit margins for commercial banks as well as other thrifts. The S&L legislation, which was recently and expeditiously cleared by the Senate, will resolve these institutions and reduce the pressure.

In the broader international arena, the position of U.S. banks has declined over the last two decades. In 1970, 7 of the world's 10 largest commercial banks, as measured by total assets, were U.S. firms. That declined to 3 of 10 in 1980 and none today. Several forces are at work, including the change in exchange rates, especially that of the yen-dollar, and the more concentrated structure of banking abroad compared to the U.S. But the restricted range of activities permitted to U.S. banks also has

played a role. The broadening of permitted commercial bank activities would enhance the competitive position of U.S. banks by stabilizing and increasing their profitability. And it would allow U.S. banks to meet their foreign competitors on a more level playing field, since a number of foreign banks operating in the U.S. are today permitted to engage in activities prohibited by Glass-Steagall to their U.S. competitors. Moreover, the experience some U.S. banks have developed abroad in these activities could be used to good effect at home.

As the financial services industry continues to evolve, it may well become clear that the distinction between commercial banks and thrifts has less economic meaning than one between smaller, "community" institutions and larger, "wholesale" institutions. That is, there may be more in common among most thrifts and the great majority of banks, all directed toward serving community, retail financial needs than between these banks and their multinational counterparts whose major focus is on the wholesale banking needs of corporations and similar institutions. If this does become the pattern of evolution, I believe it will have important implications for, and simplify the development of, legislation dealing with such issues as permitted banking activities and deposit insurance.

C. Securities Markets

Finally, how the markets for securities and related financial instruments develop has important competitive implications. The October 1987 market break revealed important weakness in both the institutional structure and regulation of these markets. Competition among the marketplaces for stocks, options, and financial futures is essential to continued capital market innovation in the face of increased pressure of global competition. But to operate efficiently and safely, these separate marketplaces must be part of a system which reflects, both in institutional structure and regulation, the economic functioning of one market.

There have been over the last year some positive developments in this area. Both the circuit breaker mechanisms developed jointly by the Chicago Mercantile Exchange (CME) and the New York Stock Exchange and the cross-margining discussions between the CME and the Chicago Board Options Exchange--initiatives of those private organizations themselves--enhance the integrity of the one market system. At the same time, little has been done to coordinate and integrate the clearing and settlement systems of these marketplaces. The October 1987 break demonstrated the brittleness of these systems and the damage to the broader financial system which could result from a rupture. An important agenda item must be work on clearance and settlement systems, to assure that the U.S. marketplaces relate effectively to one another and are integrated into the evolving global clearance and

settlement system. This issue will be high on the agenda of the Working Group on Financial Markets.

I would be happy to answer any questions the Committee might have on these or other issues.

The CHAIRMAN. Very good. We appreciate having those policy snapshots on those issues.

Let me take you down now on some areas. Some will overlap what you've just said. Some will be in addition to that. You have certainly been heavily involved in the Department's handling of the savings and loan legislation. Indeed, you have been the lead person for the Treasury, have you not?

Mr. GLAUBER. I should say I've shared that with Mr. Mullins, the Assistant Secretary for Domestic Finance.

The CHAIRMAN. Would it be fair to say that the two of you, then, as a team, have led that effort in the Treasury Department?

Mr. GLAUBER. I think that would be fair; yes.

The CHAIRMAN. Do you intend that that will continue? Can we assume that in your duties that you, with his help and others, will continue to be the lead in that area?

Mr. GLAUBER. Yes. Certainly issues that concern the S&L's fall within the range of my responsibilities.

The CHAIRMAN. What percentage of your time would you say you've been giving to that issue, say, since you got to town here, let's say January 1?

Mr. GLAUBER. I would say that it has probably occupied two-thirds to three-quarters of my time. The Secretary made it clear to me in my capacity as a consultant, which is my capacity at this time, that I should concentrate the bulk of my efforts on that.

The CHAIRMAN. Do you have a sense after the legislation passes, what portion of your time you expect to have to devote to the continued working out and oversight of the savings and loan issues?

Mr. GLAUBER. Obviously it will drop considerably, both because I will, I presume, if confirmed, take on other duties; and also because the major operating responsibility will be contained in the Resolution Trust Corporation.

So I find it difficult to estimate, but it would be obviously considerably less.

The CHAIRMAN. Would you think at least 10-15 percent of your time?

Mr. GLAUBER. I would think something on the order of 10 percent might be a reasonable estimate.

The CHAIRMAN. Now, with respect to financial modernization, including such matters as Glass-Steagall modifications—you touched in part on this in your opening statement—this committee, of course, has devoted very considerable time to that issue as well.

Will you be the senior person at Treasury with responsibility for financial modernization?

Mr. GLAUBER. Certainly that will fall into my range of responsibilities, as contrasted with Mr. Mulford, for example.

The CHAIRMAN. Well, thinking of it domestically, that will be your assignment, will it not?

Mr. GLAUBER. Yes, sir. Of course, the Deputy Secretary will have some responsibilities in this area as well.

The CHAIRMAN. But reporting to you?

Mr. GLAUBER. Yes, sir.

The CHAIRMAN. As you look forward in terms of the whole question of adjustments to the financial system, deregulation, modern-

ization, what's your estimate of the amount of time that you will likely have to devote to that part of your work?

Mr. GLAUBER. I find it very difficult to give you more than a ballpark figure, but again I would imagine that that would occupy perhaps 15 percent of my time.

The CHAIRMAN. Now, you served as the Executive Director of the Presidential Task Force on Market Mechanisms, which we think of as the Brady Commission. When the issues of market reform come up again here—and you've touched on it in your comments this morning—will you be the senior person at Treasury with responsibility for developing the positions on those issues as well?

Mr. GLAUBER. Certainly my predecessor had responsibility for chairing the Working Group on Financial Markets, which was the focus for that activity in Treasury. I have not explicitly discussed that with the Secretary and how he wants to organize it, but I would imagine that it is mostly likely to fall to me, yes.

The CHAIRMAN. It certainly seems logical. You were the person that was centrally involved in doing the work before. Is there any other place within Treasury where that would normally fall?

Mr. GLAUBER. No, sir. As I say, it fell there before and it would logically fall there again.

The CHAIRMAN. To the extent that that's the case, again I would ask you for an estimate as to the amount of time you think might be consumed by that question: the way the financial markets work, the need to devote time and attention to changes that may be needed there, monitoring that kind of activity.

Mr. GLAUBER. I would suggest something on the order of 15–20 percent probably would be a reasonable estimate, sir.

The CHAIRMAN. You mentioned also leveraged buyouts in your comments and the whole question of the degree to which changes may be needed. I know this is a matter of interest within the Administration. The Treasury Secretary has commented on this as well.

In terms of things that would relate to leveraged buyouts and things that would relate to changing of the insider trading laws, and tender offer reform laws, you mentioned the issue of pensions not being required to necessarily have to sell, to take a short-term gain if there's stock in play, in that area of the way the capital markets work and the tender offer process works as it would relate to leveraged buyouts, would that normally fall within your scope of authority as well?

Mr. GLAUBER. As you have suggested, Mr. Chairman, some portions of that clearly would. The parts that relate to securities markets. There is, of course a large part of that issue that relates to Tax Policy.

The CHAIRMAN. Absolutely.

Mr. GLAUBER. And Tax Policy does not report to me, and so it would not be directly part of my responsibility.

The CHAIRMAN. Who does Tax Policy report to?

Mr. GLAUBER. I believe it will report directly to the Deputy Secretary and, of course, to the Secretary then.

The CHAIRMAN. Right. But that does not fall within your bailiwick as you see it, the tax aspect?

Mr. GLAUBER. That is correct, sir.

The CHAIRMAN. But the market structure aspect, the rules and regulations as they relate to trading practices and so forth, would fall within your jurisdiction.

Mr. GLAUBER. I think that's fair to say, Mr. Chairman.

The CHAIRMAN. Do you have a sense as to the amount of time that that area is likely to require?

Mr. GLAUBER. It gets a little more difficult to forecast that because again there is this split between the securities markets aspects and the tax policy aspects, but I suppose 10–15 percent of my time might be spent on those portions of LBO activities which fall into my responsibilities.

The CHAIRMAN. The LBO activities that are the non-tax part.

Mr. GLAUBER. Yes, sir.

The CHAIRMAN. And you're nodding in the affirmative.

Mr. GLAUBER. I am nodding in the affirmative.

The CHAIRMAN. All right. Very good.

I have some other questions that I want to raise with you, but let me now yield to Senator Wirth.

Senator WIRTH. Thank you very much, Mr. Chairman.

Mr. Glauber, welcome. I am very pleased that the Administration has had the good judgment to take you on in this important assignment. I must say this is a little like a morning of old home week, with Mr. Mulford first and then my college classmate, Bob. So we are really pleased to have you here.

Mr. GLAUBER. Thank you, Senator.

Senator WIRTH. A couple of questions. You were, as I remember, the Executive Director of the Post-Crash Tax Force.

Mr. GLAUBER. That's correct, Senator Wirth.

Senator WIRTH. What was it formally called?

Mr. GLAUBER. It was called the Task Force on Market Mechanisms, Presidential Task Force on Market Mechanisms.

Senator WIRTH. What recommendations that came out of the Task Force have been implemented?

Mr. GLAUBER. Several of them have, Senator Wirth. First, the exchanges themselves have worked out, under the oversight of the CFTC and the SEC, a series of circuit breaker mechanisms, which was one of the major recommendations of that task force.

Those circuit breaker mechanisms have been in effect since last October. Actually, one of them was tripped into effect a month ago in Chicago. I believe that they are for just one year and will be reviewed then by the Exchanges for extension beyond that period of time.

A second focus has been on clearance and settlement systems. The Working Group on Financial Markets, which has met under the Chair of the Treasury, has focused on a number of issues—that's been one of them—and has begun in the direction of developing better systems for the coordination of clearance and settlement, although as I suggested in my statement, I think there is a great deal more work to be done in that regard.

Senator WIRTH. Just on that front, Mr. Corrigan from the New York Fed, as you know, had a very far-reaching set of recommendations. Senator Graham and I had included that in legislation, which ultimately did not pass, but that we ought to be looking at this settlements process.

I raise that only as a side bar to say that you've got a lot of support up here. Senator Bob Graham from Florida and I had both been very struck by the importance of that area, that the Corrigan recommendation seemed to be headed in the right direction. You all were touching on it. Is that going to be a priority in your bailiwick?

Mr. GLAUBER. I think it is very safe to say that is going to be certainly a priority item on the agenda of the Financial Markets Working Group with which I will be involved, at least I expect to be involved.

I believe, as I have suggested, that that's an area where we really do need to make more progress. Clearly, the experience of October 1987 uncovered some very serious structural weaknesses in that system, in those systems, and we just need to turn our attention to it.

Senator WIRTH. Are there other items that came out of the Post-Crash Working Group that are of note to be discussed this morning?

Mr. GLAUBER. There were several other items. We suggested the need for better coordination among the regulators and among these marketplaces, suggesting that this really was one market.

The Working Group has become the focus of that coordination and, as best I can see from afar, has been an effective focus for that coordination.

Senator WIRTH. That would require significantly greater coordination and of the markets between Chicago and New York. Is that right?

Mr. GLAUBER. We suggested that they really did need to be integrated in a way that reflects the economic reality; that this is really one market.

Senator WIRTH. And you're moving in that direction now at the Treasury?

Mr. GLAUBER. I believe that the existence of the Working Group is a recognition of that. The discussions on clearance and settlement, on cross-margins, on the circuit breakers, is evidence of movement in that direction. I think we need to do more, and it will be an important focus of the Working Group.

Senator WIRTH. I think that's true.

One final question in the time that I have relates to an issue that you and the chairman were briefly talking about: leveraged buyouts and the treatment of debt versus the treatment of equity. It seems to me that it's very difficult for us to get into the business of trying to decide what's a good LBO or what's a bad merger, or to make any kind of distinctions like that.

I think the evidence is overwhelming that you can't make that kind of a distinction. It's all across the block. We had a number of hearings when I chaired the subcommittee on the House side that were very extensive and I think very thorough, and you were involved in some of those.

There just aren't any conclusions that are very convincing. However, I think that one remaining major issue sits out there, and that's the treatment of debt versus equity. We are, in effect, rewarding debt it seems to me, if you look at the tax policies of the country, and we are penalizing equity.

Is that too simplistic a way of describing it, or is that a basic way that we ought to go about starting to think about this area?

Mr. GLAUBER. I believe, Senator Wirth, that we really do need to concentrate on that distinction. I believe the way to do it is to work towards integration of the tax treatment of dividends between the corporate tax system and the personal tax system so that we don't double-tax dividends, and we put them, then, on a level playing field with the way we treat debt.

The CHAIRMAN. Which would mean, then, that if you were going to do that that means you have to treat capital gains as you all have suggested.

Is part of the recommendation on capital gains that long term become defined as being a little bit longer than 6 months? Isn't long-term capital gains now 6 months in the law?

Mr. GLAUBER. Yes, it is.

Senator WIRTH. Is that your definition of what a long-term gain or loss would be?

Mr. GLAUBER. I would be very happy to see the Administration's plan for capital gains reform adopted, which would ultimately move that definition out to 3 years. I think one of the important dimensions of the Administration proposal on capital gains is to lengthen the time horizon over which investors look in making their decisions, and I think if we could make that structural change, we would both reduce the cost of equity and we would set investors looking at what I think is the right time dimension.

Senator WIRTH. I am not unsympathetic to that idea, but I don't think that is going to be done unless and in fact we also take out the enormous taxpayer reward that's out there on the debt side. The fact that this is deductible, it seems to me, just puts a huge premium out there for the conversion or equity, doesn't it?

Mr. GLAUBER. Senator, it does, but as we seek to level the field between debt and equity, I think it would be a mistake to do it in a way which increases the cost of capital for corporations by making interest nondeductible. I would much prefer to see us level that playing field by making dividends effectively deductible, because I think that is the right structure.

As we make these changes, I think we have to be conscious of the competitive position of U.S. corporations compared to other corporations in other countries. In virtually every other country with whom we trade, or the major industrial countries, their tax system integrates on the dividend side between corporations and individuals, so that they do not doubly tax dividends.

Senator WIRTH. And the contribution, on the other hand, paid by the corporation in almost every Western industrial society is significantly greater than in the United States, isn't it?

Mr. GLAUBER. It's true that in a number of them it is. But I think for us to go in a direction now of raising the cost of capital for our corporations would simply make them less competitive.

Senator WIRTH. A level playing field is always going to be something of a mirage. What's level to one person looks like the Rocky Mountains to somebody else. I understand that.

Mr. Glauber, thank you very much for being here. It is a tribute to the Administration to bring in somebody of such capacity and ability.

Thank you, Mr. Chairman.

The CHAIRMAN. Well, we like to tap the Harvard Business School whenever we can.

Senator WIRTH. I think it's the college we were talking about, not the Business School, Mr. Chairman.

The CHAIRMAN. Let me ask you this as a follow-on to what Senator Wirth was asking about leveraged buyouts. You indicate that the data is incomplete. What are we doing to get complete data? Are we making an effort to assemble enough factual information to be able to make some judgments here?

Mr. GLAUBER. I think the answer to that is yes. There have been some studies published recently, in fact one by a graduate student from the Harvard Business School, who is now at the University of Chicago, which helps increase the record.

There is just recently reported in the press, a study by William Long, who is now I guess on the staff of the Brookings Commission, which is very preliminary. And if they go down the road of their full study——

The CHAIRMAN. How about putting the Treasury to work on it? I mean why should we have to rely on graduate students, even if they do exceptional work? I mean if this is an important issue, and it clearly is, and you see it as that, why doesn't the Treasury get busy and put the data together and lead the effort to understand the problem?

Mr. GLAUBER. I think there are some things we can do. We have, in fact, been cooperating with Mr. Long for several months and encouraging him to do his work. Part, frankly, of the incompleteness of the data comes from the fact that most of these LBO's have occurred against a background of a rising economy, and so much of the discussion centers on whether or not these firms will behave in an effective manner when they come under economic pressure.

The CHAIRMAN. Are you having trouble getting money to actually do a size-up of the LBO problem?

Mr. GLAUBER. To be perfectly frank with you, Mr. Chairman, I know absolutely nothing about the budget side. We have not requested specific money to do a large-scale LBO study, so I just simply can't respond to that.

The CHAIRMAN. I think an LBO study needs to be done. I don't know that it takes a lot of money, but I think it ought to be done so that it is sufficiently independent.

Now, outside sources may or may not be independent. I think we need one that's done in the public interest, by the public, for the public, for public policy purposes, and I think we ought to get at it. I'd like to see the Treasury do it.

I don't know what it costs to do that job competently, but somebody ought to be put to work on it and we ought not to be just storm-tossed and wait for a smart graduate student to crank out a piece of work on this.

Mr. GLAUBER. As I said, this study that I understand is going to be undertaken by the Brookings Institution by Mr. Long is likely to be quite comprehensive and is likely to I think produce very revealing information.

The CHAIRMAN. We have pursued that, and our understanding is that they don't have any money over there of any consequence to

do the work. I know that there has been a great wave of privatization and private sector initiative. we've seen it in the savings and loan business over the last decade. We've seen it in the airline business. We've seen it in a lot of places. But there are some areas where I think there's a direct Government responsibility to understand what's going on and to do some serious analytical work.

You did that, in effect, in the market study effort, of course, after the crash. It might have been nice if some work had been going on before the crash, but at least it was done after the crash. I'd like to see a serious piece of work done here within the Government, sufficiently staffed by competent people, who are working on behalf of the people of the country and no outside interest group, to try to figure out what's happening here and what ought to be done about it.

So let me urge that that be done and that we not try to just hope that somebody else is going to do it somewhere else because that really isn't a sufficient answer.

Mr. GLAUBER. I understand your point, sir.

The CHAIRMAN. Now, let me ask you with respect to Resolution Trust Corporation that is going to be responsible for managing hundreds of billions of dollars of assets and disposing of them into the market, what steps do you plan to take to ensure that there's no favoritism or political influence, or anything else, in a process that will be developed here, where inherently I think that's always a risk when you've got a task of this size to handle?

Mr. GLAUBER. We certainly do believe that the taxpayers have a right, with their money being used, to be certain that this proceeds efficiently, without political favoritism, of course.

What we have done is recommended in our legislation an oversight board, composed of the Secretary of the Treasury, the Attorney General, and the Chairman of the Federal Reserve, to act as a monitor, an overseer, an auditor, of the performance of these resolution functions.

As this legislation has passed through first the Senate and now the House, it has been modified in a number of ways. The Board has been changed in both the Senate side, as of course you know, sir, and now also changed differently on the House side.

It is clear that we are going to have to resolve these differences and do some simplification and fixing, I think, in conference. But an important element of that is going to be, I believe should be, the oversight by these senior officials who will assure the taxpayer that the money is being spent efficiently and fairly.

The CHAIRMAN. Well, we clearly have to establish that. One of the problems is that any time you take officials from just one administration, if that constitutes the whole body, that automatically gives it a certain tilt and character.

There is a view of many of us that we want to have an independent element. You know, sometimes we balance these boards by requiring people of different parties or that we have people in and out of the Government to constitute a blend, but to find some way to really give us some safeguard that there will be an inherent fairness and integrity in the system, and so it will stand up to public scrutiny.

We've got a problem, as you know, that has just developed in the Department of Housing and Urban Development with these mod rehab funds where it now appears that people who were well-connected, even people who were former Cabinet officers, received very, very large fees, in the hundreds of thousands of dollars, for basically doing nothing except perhaps a single phone call. It sure has the very clear impression of influence peddling or inside deals, in a sense, the looting of the money.

I don't suggest that that is going to happen here, but I think we've got to have in a program of this size, unprecedented in our national history, arrangements that are so clearly laid out and spelled out, that the full light of day is on this thing and there's an impartiality and a professional competence and a detachment that really insulates it from any kind of political tilt or favoritism of any sort.

Do you have any more to offer us on that at this point? It seems to me we're going to have to decide those things rather quickly because this problem is upon us. This isn't something that's way off in the future.

Mr. GLAUBER. It certainly is upon us and indeed our hope is that this legislation will move quickly so that it will be upon us even sooner. I think on the issue of oversight, the appropriate structure is the one we've recommended. I believe a board chaired by the Secretary of the Treasurer, with the Attorney General and the Chairman of the Federal Reserve, is an oversight function in which the taxpayers can have confidence.

In terms of the matter of efficiency and functioning, as we have stated in our legislation, the FDIC would be looked to as the primary operator, contractor, of the RTC; and it is, after all, the largest, the most effective, most professional workout body that we have for financial institutions, and I think it's the appropriate place to look for primary responsibility.

The CHAIRMAN. Give us a sense as to how many full-time employees the RTC is likely to have, separate from any Federal employee that are borrowed from Treasury or some other place in the Government.

Mr. GLAUBER. I can't give you a precise answer, but we certainly believe it should be a lean organization and one that does not exceed 100 full-time employees.

The CHAIRMAN. Does not exceed 100.

Mr. GLAUBER. Yes.

The CHAIRMAN. So would one infer from that, then—I mean how do you get the work done unless you do a lot of outside contracting?

Mr. GLAUBER. That's an appropriate assumption. As we have said before, the RTC is going to be primarily a contract giver and its major function will be to oversee contractors whose task it is to dispose of these assets and resolve these institutions, the FDIC again being the primary contractor.

The CHAIRMAN. Have you been following the stories on this mod rehab problem that the Inspector General has discovered in the Department of Housing and Urban Development?

Mr. GLAUBER. Not at a greater level of detail than that which you have just——

The CHAIRMAN. All right. I'd like you to make it a point to take a close look at it, because what happened there was that it's a contracting type situation, and it's the question of who gets the contract, who gets to do it, who doesn't, and what are the rates and so forth.

We are pursuing that now because there's a very bad odor about what happened, and Secretary Kemp, to his credit, has suspended the program because he found it so troubling in terms of the data that has been developed here.

But I want to serve notice now that this committee will go to war with any process that we see that has the slightest hint or appearance of anything that smacks of inside deals, favoritism. Bureaucracies can sometimes do that, despite the best of intentions of people that may be in the upper reaches of the bureaucracy. But what I want is an assurance from you that as we construct this system and the safeguards, that we have iron disciplines in place that can really prevent the kind of abuse that I think otherwise would be very likely to happen, or this kind of a situation, because it is so extraordinary and it's spread all across the country, is inherently susceptible to that kind of a problem.

Mr. GLAUBER. I am certainly prepared to give you those assurances. We are very sensitive to that issue and I can assure you the Secretary of the Treasury will be in the trenches with you.

The CHAIRMAN. I think this is going to be one of the real tests of the administration as to whether or not it can be so hard-boiled and put such a system with rectitude in it from top to bottom and from left to right, and up and down, and every direction, to prevent that from happening. We intend to apply a scouring oversight from this committee as well because of the risks that I have already stated.

Mr. GLAUBER. We, of course, welcome that oversight, Mr. Chairman.

The CHAIRMAN. According to an Associate Director in the FDIC's Division of Liquidation, the FDIC sold about $250 million in real estate in 1988. My understanding is that the FDIC employs about 3,000 people to manage and liquidate its assets.

Mr. Richard Breeden at the White House recently estimated that $60 to $100 billion of real estate will be in the RTC's portfolio, which in the overall is estimated to be somewhere between $300 billion and $500 billion of total thrift assets.

If you take and relate one to the other, if what the FDIC has managed to do with 3,000 people managing its assets is to basically unwind and sell off by one means or another, $250 million in assets a year, and we are now faced with a figure of $60 to $100 billion in just real estates, not to mention all the rest, if we were going to see a disposition rate that was at that level, it ought to take us about 240 years or longer to just wind through the real estate aspect of this thing.

I take the time to say this because I think this is such an incredible problem, it's such an extraordinary size that I don't know that anybody yet understands it. We can't understand it because we have no historic parallel. I'm not sure the press understands it, and the public won't understand it until the press sees it and sort of helps the rest of us get the story out there.

But what do we intend to do? I mean if the FDIC, with 3,000 people, have only been able to sort of work out $250 million worth a year, how do we propose to take and really do this job?

Mr. GLAUBER. I think the concepts are different, Mr. Chairman.

The CHAIRMAN. And with a group of less than 100 people.

Mr. GLAUBER. We look upon the RTC as an organization that will be an administrator of contracts, not an operator of those contracts. The FDIC, to a great extent, is an operating entity that is responsible for the sale of those real estate assets.

So it is our intention to devolve upon the FDIC and on other private sector entities, the responsibility for the actual liquidation and sale of those assets. So I don't think it's quite fair to compare the 3,000 employees of the FDIC against the number of employees at the RTC, since again the function of the RTC is going to be to administer contracts and to operate through contractors.

The CHAIRMAN. Do we even know that contractors in the amounts and types needed are out there to facilitate this kind of an enormous workout situation?

Mr. GLAUBER. Again, the FDIC is the primary contractor. Beyond that, we do believe that the private sector is going to rise to this calling. I am encouraged by the newspaper reports this morning that Solomon Brothers and Blackstone Partners are in the process of raising a substantial amount of money for simply the purpose of bidding on these assets.

I think this is the first of a large number of such partnerships that we are likely to see. We believe that when the thrift industry is restructured as it will be, that it's going to be an attractive industry, a profitable industry, and will be one that will attract capital.

The CHAIRMAN. I want to move on from this, but it's such an important issue, and because of all the preoccupation with the mechanics of taking and restructuring the savings and loan system, we really have not yet had the opportunity to move the focus forward to the asset disposition problem. This is probably as long a discussion as we've had on it in a public setting such as this yet.

But that is a gigantic issue that becomes center stage here, and with all the aspects to it and dimensions that we've already discussed. It is still not clear to me how the private sector people are going to be brought in. I can see—I read the story this morning as well about the investment consortium that has been formed by Solomon Brothers and the others that you mentioned—but what I am concerned about is the public—these are public assets, and so this is the public's money, and people up and down the street of America, in fact, own these assets and they are entitled to every last penny of value.

I am very much concerned with that because of the sheer size of the task, that we may end up not being able to create a system that can get full value or fair value out of these assets. And to the extent that we fall short in that area, you not only have the problem of favoritism and somebody getting an inside track and getting rich by buying undervalued assets on some special basis or somehow getting access to them, and so you've got that problem on the one hand.

On the other hand, you have the situation where if we end up selling these assets at anything less than their full true value, we're cheating the public a second time, because I think the public is being cheated in the first instance because they're having to cough up all this money to cover the deposit insurance because of a breakdown of a system that they really had nothing to do with, but they're being asked to shoulder the bulk of the cost of that.

If they don't get the full value out of the assets, you know, it compounds the felony. I must say that I get the sense that there isn't a very clear view yet within the Administration as to exactly how this is going to be done. I still don't, even after this discussion, have a clear sense as to how the private sector players are going to be identified and brought into the act.

Do you have a view of that?

Mr. GLAUBER. First, I agree with you that it is a very, very large undertaking and a daunting challenge. I think it would be a mistake for us to construct a large bureaucracy that perpetuated itself over a long period of time in order to undertake this task.

I think, to the question of how these contractors will identify themselves, I think we have seen the first step already. They will come forward. They will raise money, they will identify themselves, because I think it is going to be in their interest to bid on these properties.

We need to protect the taxpayer and make certain that we get the full amount. We can do that, I think, through the use of participation contracts with these private entities to make certain that they have the motivation to manage these properties most efficiently and ultimately resell them at the best prices, and that we participate with them as their partners in whatever profits they make.

The CHAIRMAN. Am I right—I don't single them out, I want to say this, because we've got the current illustration in the news today—am I correct in recalling that the Blackstone Company was involved in representing the Bank Board in several of the December deals that were done?

Mr. GLAUBER. I believe that is correct. I believe they were adviser on some specific transactions that the Bank Board undertook. The Blackstone Company is a partnership formed of Mr. Peterson, former Chairman of Lehman Brothers and Secretary of Commerce.

The CHAIRMAN. I am very much concerned about both the appearance and even more so if there were the reality of a group of entities who became sort of inside players and somehow, by virtue of their involvement in this unfolding problem over a period of time, sort of cash in on the problem all the way along.

I don't mean by that to draw a negative inference about this firm. I'm not in a position to do that and it's not my intention to do that.

But I am concerned about the question of whether you see a pattern develop over a period of time where well-positioned entities or inside players sort of feed off this problem all the way through. We've seen this in terms of other stories that have run on people who got involved in doing these deals over a period, even people who used to work on the Bank Board themselves, were actually

there, helped set the rules, then went out into the private sector and made a killing on sort of how these things were later done.

I think there has been so much improper activity and incompetence and stealing in all forms that have gone in the savings and loan problem, that we ought to have laws in place that would administer punishments that are so severe that they would sort of go off the scale in terms of anybody that tries to cash in on this problem from this point forward.

So I hope by means of this discussion, this will help us create together the sensitivity about how this is going to have to be put together, and if you have to hire additional people, hire them. We're talking about hundreds of billions of dollars of public assets here, and I want every last dollar of value realized from these assets. And if you can't find good people, then keep looking until you find good people, people who are absolutely devoted to the public interest. If you've got to go out and hire the best property management people that can be found in the country, who don't have any prior history or conflict of interest in these things, to come in and have special operating authority over a period of time to do these things, then you may have to make some arrangements of that kind.

But I think it's essential that this be done out into the light of day and that it be done to the very highest standards of competence and ethical propriety that we can establish here.

Mr. GLAUBER. It will surely be done in the light of day. The Administration shares your concern and your motivation. We want to make certain that that the taxpayer pays no more to take care of this problem than is absolutely necessary.

The CHAIRMAN. Do you have any view as to whether or not we should make any differentiation as to whether foreign investors be treated any differently in coming in and buying off large chunks of these assets?

Mr. GLAUBER. I think we will minimize the cost if we can attract the largest number of bidders, and I would not make a distinction between one and the other.

The CHAIRMAN. There is some concern in some quarters that we may see foreign consortiums come in and see this as an opportunity, because you've got a market overload problem, to come in and buy up a lot of very valuable assets at a fraction of their value in a more normal market situation, and that you would see ownership then pass into foreign hands at a time that is just sort of a depressed market circumstance. But you have no particular concern about that?

Mr. GLAUBER. I believe that the bidding process is going to be our defense against anybody buying these things at an unfairly low price, that we ought to attract as many bidders as we can, subject them to the same scrutiny to make certain that they are bidders in whom we have confidence, require the same kind of earnest money from them, and the same kind of participation contracts with them.

The CHAIRMAN. I want to move to several other things this morning. I notice that the Ways and Means Committee in the House has now voted, at least in their first vote, to put the FSLIC financing on the budget and to finance the bonds directly.

Has this caused any shift in thinking in the Treasury Department? Is that idea beginning to look a little more attractive to you?

Mr. GLAUBER. We continue to believe that that is a mistaken direction. We believe that the financing plan proposed originally by the Administration and passed by the Senate and by this committee is the right approach. We believe that in the end, it will be a less expensive financing approach than one which puts the financing on the budget by having the Treasury undertake the sale of the bonds.

The CHAIRMAN. Well, as you know, we've had a strong difference of opinion about that, and we've debated that back and forth, and we've voted on it here in the Senate. As I read the stories about the continuing withdrawal from the savings and loans, which are a disturbing fact, and just the time that is elapsing, we have worked very hard to try to meet an accelerated time schedule in terms of getting this legislation enacted, as you know, and we continue to feel the same sense of urgency that I know the Administration does—but let's say that we get all the way through this process and we've got everything worked out, and the will of the Congress—we've not seen the House as a whole act yet, but certainly they are as important in their view as we are in the Senate, we had a closely divided view on that financing issue in the Senate—but if we come on through with this thing and the House takes its position and the final bill that lands on the President's desk is acceptable in every other regard except for the fact that you may not prefer the financing mechanism, and with time elapsing and the losses mounting and the withdrawals increasing and so forth, does it make any sense for the Administration to think about vetoing the bill if it should come in that form?

Mr. GLAUBER. Mr. Chairman, we too, of course, are very conscious about the cost of delay. The Senate surely did move through this legislation very, very rapidly under your leadership. I think the issue that has to be weighed against that is the importance that we attach to maintaining the fiscal discipline of the Gramm-Rudman-Hollings system, and we believe that a financing plan of the sort proposed by Ways and Means would just punch a gaping hole in that fiscal discipline and, down the road, would cost us many, many billions of dollars.

So that is why, in fact, we have said on a number of occasions now in the last several days, that we hope that the House will pull back from this initiative, will not subject this bill to the kind of delay that might arise if it goes down that road.

We think that the financing plan we have proposed is the right one. It is the one adopted by the Senate. If the House will adopt a similar financing plan, we can move through this legislation very rapidly as we both want to do.

The CHAIRMAN. If we end up here—I don't know where we are going to end up because I can't predict what the House in its wisdom will do here when it finishes with the bill—but if we end up with a bill in the end that is acceptable in all regards and well balanced, with the exception of the financing, and put the bill on the President's desk, I would certainly think it unwise to be thinking about a veto when we've got an issue of this consequence.

I might just say also for the record, I've got a copy of a story here that you may have seen The Bond Buyer on April 28—and they are pretty sophisticated when it comes to financial markets—and they have written a major story where they don't think your financing plan is the best financing plan. The Washington Post editorialized on it again yesterday. And as you may know, the Wall Street Journal has editorialized that they prefer the direct financing plan rather than the Administration's plan, as does the New York Times, I am told again today, and a host of other people.

So there is a division of professional opinion, let it be said, just on that issue. I'm not here to redebate that today. But I guess my thought would be this: that is, that we're going to have to—you know, it's the nature of the legislative process that we're going to have to work this thing out. I don't presume the final form that it's going to be in. I think we've tried to work to develop a consensus here in the Senate so that we could have a good, solid, well-balanced bill that would work.

There have been close votes on some of the issues, but I would hope that when we finish and we come out of the conference, and we've got a bill, and we send it down to the White House, that if anybody is going to think about veto, you better think about it long and hard because I really think that would be a serious, serious error.

Mr. GLAUBER. This is a very, very difficult situation because there are in my view, I think in the Administration's view, fundamental issues here which go beyond the S&L legislation and deal with the fiscal discipline of Gramm-Rudman-Hollings.

The CHAIRMAN. Just one other thought on it. Did you happen to see Senator—you mentioned Gramm-Rudman-Hollings, and in reference to the Hollings of Gramm-Rudman-Hollings, he often gets left off these days because he has become a very strong dissenter as to what's happened to the process. I don't know if you happened to see his op-ed feature in The Washington Post of, I think, two Sundays ago. If you have not seen it, I want to recommend it to you. It's an excellent piece. In fact, I felt so strongly about it, I put it in The Congressional Record.

In effect, what Hollings of Gramm-Rudman-Hollings does is debunk the so-called notion that we are maintaining fiscal discipline. In fact, the essence of his piece is that through a variety of accounting tricks and off-budget, on-budget, shifting things backward, forward, mislabeling things and so forth, that we have basically rendered the process meaningless. And there are many people around here who think that. I certainly am of that view myself. I did not happen to be a supporter of that Gramm-Rudman-Hollings process in the beginning because I felt that it was susceptible to exactly what we've seen it turn into.

But I think it is important that we continue to work together on this because we want to have a good solid FSLIC restructuring bill through the mill and on the President's desk at the earliest moment. And it continues to be and will continue to be the absolute top driving priority of this Committee and of this Senator until we get it down.

Mr. GLAUBER. Mr. Chairman, I believe it's proper to say that certainly on our side, we believe we've had a very, very cooperative

experience with you, your committee, and your staff and we look forward to continued cooperation with you.

The CHAIRMAN. I want to just touch on a couple of other things here. I'm going to give you some questions to respond to for the record, but I am very much interested in what's happened to the Working Group on the market break and what form it's in today, who's on it, what's happening, does it exist anymore?

We have seen some changes, as you say, that have happened since. They are quite modest, I think, in relationship to what you and your other participants in the early study recommended. Obviously, market conditions change all the time and so we always find ourselves in a different situation than what may have existed before. But what is the status of the Working Group, who's on it, what's it doing, when are we going to hear from it again, et cetera?

Mr. GLAUBER. It's the same old people, institutionally the same people: the Chairman of the CFTC, the Chairman of the SEC, the Chairman of the Federal Reserve, and the Secretary of the Treasury or his designee. We have a staff meeting of the Working Group scheduled for either late next week or the beginning of the week after, with an agenda to pursue a number of the issues before us. We actually, in fact, had a meeting scheduled last week, and the S&L legislation preempted that meeting.

So it is alive and well. It has an important agenda, and we intend to pursue that. As you know, Mr. Chairman, these issues are particular issues of importance to the Secretary.

The CHAIRMAN. Let me ask you your own personal assessment of the current condition of the securities markets.

Mr. GLAUBER. Well, I think we've made some progress since the October 1987 experience. I think it is proper to say that there still is some investor concern. The volume on these markets is down from what it was before that time. And I think there are things still that we need to do.

What I would put at the top of that list, as I suggested a few moments ago, is the issue of clearance and settlement. It is perhaps the most important unworked part of the agenda. It is also in many ways the least interesting. I've given speeches on this subject, and you can watch people's eyes glaze over as you start to talk about it, and they beg you not to talk much longer.

I'll spare you much more of it right now.

The CHAIRMAN. But you put that at the top of the list, clearance and settlement?

Mr. GLAUBER. I do indeed.

The CHAIRMAN. What's second on the list?

Mr. GLAUBER. I think second on the list is beginning to understand how our markets can evolve together in the face of the reality of a very competitive international marketplace. It is going to require a better understanding of how electronics fit with market-making on these exchanges, how they relate one to another, and how they can operate in a world where we're going to eventually have 24-hour markets in a number of places.

So I would put an understanding of the posture of our marketplaces vis-a-vis their global competitors, which will involve an understanding of electronics in these markets as an important issue.

The CHAIRMAN. Are there others you would want to enumerate a list of key issues here that come to mind?

Mr. GLAUBER. I think, beyond that, we've got the very specific issue of what will be done about the circuit breaker mechanisms. As I said earlier, these have been put in place for a year. I think we should investigate those, and I think that we're going to have to decide, in discussions between the various regulators and the exchanges, what to do about those.

I think they have been a reassuring factor for market participants, and I think that it's something that will engage our time.

The CHAIRMAN. What about the cross-connect between the underlying securities markets and the futures markets? Where do we think we are?

Mr. GLAUBER. Cross-connect in what sense, Mr. Chairman?

The CHAIRMAN. How these markets work in conjunction with one another and the degree to which we need to understand that better, that there needs to be adjustments in those processes. I would be just interested in your sense as to where we are. Is that a matter of concern? Is that something that you're looking at? Or is that something that you're not much concerned about?

Mr. GLAUBER. I think cross-connect, of course, is at the center of the issue. As I suggested a few moments ago, this really is one market. And there have been a number of initiatives that have in fact been reflective of those cross-connects.

One of them is the whole circuit breaker mechanism. We said from the beginning that circuit breakers should reflect the fact that these are integrated marketplaces, and indeed these circuit breakers do. They are coordinated across those markets.

The whole clearance and settlement issue is again an evidence of inter-connect. Cross-margining discussions that have gone on between the CME and the CBOE again are evidence of cross-connects. So there is a good deal going on. I think there needs to be a good deal more because again, economically, these are one market.

The CHAIRMAN. So will that be on the issues, then, that your group looks at, would you say?

Mr. GLAUBER. In a sense, it stands in the background of most of the important issues when we talked. A major issue is clearance and settlement. The need for integration in clearance and settlement, for coordination of the clearance and settlement process, is evidence of what you characterized as cross-connects, and a reflection of the fact that this really economically is one market.

The CHAIRMAN. In terms of the whole takeover process and the tender offer process, we've worked on that in conjunction with insider trading changes and other things in this committee over a length of time.

When you look at the leveraged buyout activity which is fostered in part by the way the tender offer process works, and who the new players of the game are, and how capital gets assembled, properly or improperly, to go in and sort of mount a takeover effort on a company, is that something else that falls within the scope of your work or not?

Mr. GLAUBER. I believe that legislative initiatives that deal with those issues would fall on the agenda of the Working Group and therefore fall within the realm of my work, yes.

The CHAIRMAN. Would you be the principal line officer, then, within the Treasury Department, responsible for thinking through those questions and making recommendations in that area?

Mr. GLAUBER. I think, assuming that I follow my predecessor's role with the Working Group, I think the answer to that would be yes.

The CHAIRMAN. But you are starting with that presumption? I mean you presume that that will be the case.

Mr. GLAUBER. Yes.

The CHAIRMAN. We would be interested in working with you on that. As you know, this committee has done a lot of work in that area, and obviously there are a lot of unanswered questions even now in the area of the tender offer process.

I want to just briefly touch on the question of financial modernization. There are different euphemisms that can be used for it. You've been a consultant to at least one major U.S. bank which has been in the forefront of wanting to repeal Glass-Steagall.

What is your view on Glass-Steagall? Do you think it ought to be repealed or not?

Mr. GLAUBER. I think that the initiatives taken last year were steps in the right direction. I think that we really do need to examine that law in light of the issue of the competitiveness of our institutions vis-a-vis other worldwide institutions.

I think, generally speaking, there would be value in reducing those restrictions on commercial banks. I think the values would be several. It would, I think, stabilize the earnings of our commercial banks. It would, I think, raise them as well. It would benefit consumers by making available to them a wider range of products. It would lower the cost of underwriting certain municipal securities. And, finally, and in many ways of perhaps greatest importance, it would let our financial institutions, our commercial banks, meet their foreign competitors on a more level playing field.

The short answer is I think that these are, generally speaking, initiatives in the right direction. There are obviously details that need to be worked out, and I must tell you that some of the details are things of which I am not fully in possession.

The CHAIRMAN. Will you be the person that will be responsible for coordinating whatever policy recommendations come out of the Treasury Department in this area?

Mr. GLAUBER. Yes. The answer to that is yes.

The CHAIRMAN. But I take it at the moment there is no immediate time table as to when that might come, partly because you're tied up on other major issues, the savings and loan issue obviously paramount among those.

Mr. GLAUBER. Yes, I think that simply is the answer. We have really, in the area of financial institutions, been devoting essentially all of our time to the savings and loan legislation.

The CHAIRMAN. We've been doing the same thing.

So one assumes, then, that once that package and that legislative solution or remedy is in place, that you will then be in a position to move on to other things as will we here.

Do you see any major soft spots in the financial services industry? You have a very extensive background in this area. But as you look ahead, are there things out there that, whether they happen

to fall within Federal jurisdiction directly or not, that give you an uneasy or queasy feeling?

Let me just mention a couple that some stories are written about. Some people express a concern about the health of the insurance industry because of some of the types of financial issues and problems that may exist or be building up out there. Some raise questions about the credit union industry. And there are a whole host of others. I don't mean to just list those, but I list those as illustrations.

Can you give me a sense as to any other areas of the financial services industry, looking ahead, that you have some concern about and the Treasury will in due course take a close look at?

Mr. GLAUBER. I would give you two. One of them is one you mentioned—credit unions. As you know, credit unions played a part in the original legislation introduced on the S&L issue by the administration, and I think we have to continue to watch the evolution of these institutions.

This is, in fact, the fastest-growing set of depository institutions that there is.

The CHAIRMAN. Will that fall within your jurisdiction within the Treasury Department?

Mr. GLAUBER. I presume the answer to that is yes.

The CHAIRMAN. Excuse me. Go ahead.

Mr. GLAUBER. The other is an issue that we touched on a few minutes ago, and that is the LBO loans that have been advanced by commercial banks. Loans to highly-leveraged corporations could potentially be a problem. I think we need to understand it better.

The Controller of the Currency has just published a report in which they've looked at national banks and their role in advancing money to highly leveraged corporations, and they conclude that there really is not a great deal of basis for concern.

I think we need to look beyond the national banks at some of the smaller State-chartered banks, large banks that are not national banks, and understand better whether there is any reason to be concerned about that exposure.

The CHAIRMAN. What about insurance companies? Might they not have money at risk out there as well? Or do you just take that off the radar screen because insurance companies are regulated at the State level?

Mr. GLAUBER. I concentrated my comments on banks because the primary regulation, as you suggest, of insurance companies is not a Federal regulatory requirement or authority. I think insurance companies are something we ought to look at as well.

The CHAIRMAN. What about junk bonds generally, high-yield bonds? They travel under different names as well. But is that an area that has any particular level of concern to you?

Mr. GLAUBER. My interest in junk bonds is mainly, frankly, my concern would be mainly in the direction of who holds those. To the extent that they're held by individuals through diversified mutual funds, I have less concern. When they are held in large amounts by certain kinds of depository institutions, thrifts, that seems to be a subject of some concern, particularly concern for the amount of capital that they have.

As you know, our legislation recommended that certain kinds of capital requirements be applied to the holdings of activities that didn't conform to national bank activities.

The CHAIRMAN. We have seen and we have addressed the issue in the savings and loan legislation of the degree to which junk bonds are ending up as a major element in asset holdings of savings and loans. It varies from State to State, as you know.

But there is now data accumulating that indicates that insurance companies in many cases seem to be reaching for the higher yields and have therefore become major buyers and accumulators of junk bonds. Now, that may or may not have a long-term implication, but I think it appears to be a developing pattern.

Have you seen that? Is that a matter of concern to you?

Mr. GLAUBER. To be frank, Mr. Chairman, the insurance industry in fact is not one that I have studied in great depth. I am broadly aware of the trends that you suggested, but it is a matter that requires some more study by me and by us.

The CHAIRMAN. I am just wondering if the whole junk bond issue, the part of it that you have a concern about, and that is in effect who holds the junk bonds—would you be the part of the Government—I assume you would be the part of the Government that would undertake to assess that and try to make some sense out of it. Is that not right?

Mr. GLAUBER. I think the assessments, Mr. Chairman, would come from a number of different directions. I am sure that the SEC has some concern for these in terms of the registration and information that's distributed when they're sold.

Our major interest I think at Treasury would be in terms of certain kinds of holders, particularly insured depositories as holders of these bonds, so I think it would come more from the holder rather than from the entity of the junk bonds themselves.

The CHAIRMAN. Just a comment, and then I want to ask one other question, and then we will be finished here today. That is this: shocks to the financial system. I think confidence and psychology is obviously very important, always is important as it relates to financial markets and just the buoyancy of the economy and people's expectations and so forth.

We have had some real jolts. We had the stock market crash, which we have spent a great deal of time analyzing how it happened and what might be done to forestall that kind of thing from happening again in the future. We have had the savings and loan catastrophe occur here, which is a financial structure problem. We have the Third World debt problem which is very much a major issue—it is now a major initiative by the Secretary himself to try to take and move that problem—the news today about Citibank's decision with respect to Ecuador and so forth. So that is a hot front-burner issue.

We have a host of other questions. You obviously have a concern, many people do, this committee does, about financial modernization, how do we gear into the rest of the world, the global market system, global financial system and so forth?

I am very much of the mind to feel that what we ought to be doing is figuring out what crises or problems might be in the making that we can diffuse now so that we don't have more shocks

that hit us later. Now, foresight is always difficult to have in these situations. But I would hope that within the Treasury Department—and it would be the desire of this committee to want to work with you in these areas as they relate to the matters that fall within the jurisdiction of this committee—to try to look ahead and see what trend lines we're riding that may be taking us toward unhappy consequences that could administer additional jolts and shocks to the financial system, that could either force interest rate gyrations or other problems, radical currency evaluation shifts, other things that become perhaps secondary effects but very economically disruptive and damaging effects, and to see if we can't try to take—if we see that we're on a trend line that's taking us in the wrong direction, try to understand what is causing that and how we undertake to do some things differently now so that we don't have these terrible shocks.

We had a hearing here one day when John Shad was still the head of the SEC, where he was asked a question—in fact, I asked him the question—given all of the developments that we saw in the markets at those times, if it was feasible to imagine that the market might go down as much as 500 points in a single day.

Well, we were off by 8 points. It went down 508 points. But he really thought that was way, way outside the bounds of anything that could conceivably happen, and within a matter of about 6 months, lo and behold, that very thing did take place.

So even very sophisticated people who have spent a long time in that business, the longest-serving SEC Commissioner, was obviously not in a mind frame to even imagine that something like that could happen and then, lo and behold, within a relatively short period of time, that very event did happen.

I would hope that, partly because of your academic background and the kind of analytical skill that you bring, that we can, as we work through the crises that have been left over from past circumstances, that we try to anticipate other trend lines that are running against us and see if we can't get ahead of the curve.

This committee will be active in wanting to work and think with you constructively as to where we can do that.

Mr. GLAUBER. I look forward to that, Mr. Chairman.

The CHAIRMAN. One other thing here. That is, would you communicate to the Secretary, our interest in having him appear before the committee as soon as the Treasury feels comfortable and is prepared to testify on the implications for the United States of Europe 1992 as they relate to the whole host of issues that we have been discussing here today?

I don't know whether you have any thoughts on that, and if you are involved in aspects of it. Obviously, the financial services part, it would seem to me, falls directly in your area of responsibility. But I don't know if you have any thought that you want to give but, if so, I would be pleased to hear it.

Mr. GLAUBER. I think it would be a little premature for me to do so at this point, but I will certainly communicate the committee's interest to the Secretary.

The CHAIRMAN. Very good.

Let me just conclude by saying that I appreciate your testimony today. There are some other issues that I will want to ask you to

respond to for the record and will give you those within a day's period of time because we don't want to delay things here.

But one of those questions will relate to the role of foreign firms moving into the U.S. financial structure and buying up either pieces or controlling interests of companies and, as foreign interests become loaded with dollars off the trade deficit and the adverse flow of our national balance sheet, what that means, what the implications might be to have foreign interests taking a larger and larger role in what previously were domestically run and operated major financial institutions. So we will have a question for you on that.

I will just finish by saying that, for my part, I'm pleased you are willing to come into Government. You have served with distinction for many years at the Harvard Business School and in other capacities, and it is important that we get good people willing to serve. These are not easy jobs.

You have undertaken, with respect to your financial affairs, to put them in a qualified line trust. I appreciate the fact that you are willing to come in and take on a major assignment in Government at a time when we've got a lot of very tough problems to work through.

As I say, we have gotten off with a very active working relationship on the savings and loan issue, but I think it lays a foundation for a host of other issues that we will be working on together. And I know I express the view of the committee as a whole—other members are at a variety of other hearings this morning—but there is great interest in the work that you will be doing, and I express that on behalf of my colleagues as well as myself.

Mr. GLAUBER. I thank you for those kind words and I look forward to working with you and the committee.

The CHAIRMAN. Very good. Thank you for your testimony today.

The committee stands in recess.

[Whereupon, at 11:22 a.m., the hearing was adjourned.]

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